

**Appendix B**

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<b>GSEs' Entry Into, and Participation in, the Subprime or Non-Traditional Loan Market</b>	
<b>Zhao Tr. at 658:2-660:12</b>	<p>658:2 Q. (BY MR. SACCA) Let me show you what we're  658:3 marking as Exhibit 3567, FHFA05693580 through 81.  658:4 The bottom e-mail on the first page is  658:5 from Fan Xu -- how do you pronounce it?  658:6 A. Fan Xu, yes.  658:7 Q. Xu.  658:8 -- to a group of people.  658:9 Do you know who those people are in the  658:10 "To" line?  658:11 A. I know some of them. Like Gordon is her  658:12 boss. Luis is -- may be her direct boss, like as a  658:13 lower-level boss, or may be her colleague. They're  658:14 all -- yeah, some of them are colleagues. They're  658:15 all -- most of -- the names I know are researchers in  658:16 Credit Research Department. Except Vanessa, actually.  658:17 Vanessa is in David Gussmann's organization.  658:18 Q. Okay. So these are colleagues of hers at  658:19 Fannie Mae?  658:20 A. It looks like it, yeah.  658:21 Q. And she's sending them an article from that  658:22 day's Wall Street Journal, October 30, 2008, titled  658:23 "Ex-Fannie Mae Chief Mudd: Should Have Said 'No' More  658:24 Often"?  658:25 A. Yeah.</p> <p>659:1 Q. And you see the first line of the article is  659:2 "Daniel Mudd says he should have said 'no' more often  659:3 when he was chief executive officer of Fannie Mae"?  659:4 A. Yeah, I saw that.  659:5 Q. And then if you look on the second page of  659:6 the e-mail, the first reported question there from the  659:7 Wall Street Journal was "What were your main  659:8 mistakes?"  659:9 And Mr. Mudd's answer was, "I wish I'd  659:10 said 'no' to more of the things the company was asked  659:11 to do. We were asked -- or required -- to expand  659:12 lending, to conserve capital while providing  659:13 liquidity, to meet housing goals for the underserved,  659:14 to serve shareholders and homeowners alike. In a  659:15 crisis of these proportions, something had to give. I  659:16 should have gone to the government and gotten a clear</p>

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	<p>659:17 answer to the question: What do you want -- more  659:18 capital or more lending?  659:19 "In 20/20 hindsight, I can go through  659:20 and pick out loans I'd rather not have on the books."  659:21 Ms. Xu sent you this e-mail also on  659:22 October -- or this article also on October 30th, and  659:23 she said "Have you seen this? Exactly as what you  659:24 said - the executives should have said 'No' which what  659:25 they are paid for."</p> <p>660:1 Had you been taking the position that  660:2 Fannie Mae should have said no to having certain loans  660:3 on its books?</p> <p>660:5 A. I don't remember the conversation I had  660:6 with -- with Fan I guess. Have I been taking the -- I  660:7 mean, I don't remember the specific conversation she  660:8 was referring to.  660:9 In terms of if you ask me have I taken  660:10 the position to say no, I -- I would say probably yes  660:11 after the crisis, like in '09 time frame, or '08, '09  660:12 time frame.</p>
<b>Syron Tr. at 255:6-261:24</b>	<p>255:6 Q. Mr. Syron, you have in front  255:7 of you an exhibit we've marked as 34619,  255:8 which I think you can see is an email  255:9 from David Andrukonis to you among  255:10 others, dated April 26, 2004?  255:11 A. Yes, it isn't to me, I'm cc'd.  255:12 Q. I stand corrected. You're  255:13 cc'd. Do you recall this email?  255:14 A. I have to look at it. I don't  255:15 remember.  255:16 Q. Do you see at the beginning of  255:17 the second paragraph he says "The first  255:18 issue is the slippery slope issue we face  255:19 constantly. As I said in the meeting I  255:20 would be interested in how we would  255:21 answer the question of what wouldn't we  255:22 do to achieve market share."  255:23 Do you see that?  255:24 A. Yes.  255:25 Q. Do you remember having</p>

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256:2 discussions with Mr. Andrukonis about  
 256:3 this topic?  
 256:4 A. About the SISA issue I do.  
 256:5 Q. SISA and NINA?  
 256:6 A. NINA, yes.  
 256:7 Q. Just for the record, what does  
 256:8 SISA and NINA stand for?  
 256:9 A. SISA is, I remember mostly  
 256:10 about SISA, I don't remember much about  
 256:11 NINA. SISA is stated income/stated  
 256:12 assets. NINA is no income/no assets.  
 256:13 Q. And those are documentation  
 256:14 types of subprime loans?

256:18 A. I believe so.  
 256:19 Q. So stated income/stated assets  
 256:20 is a type of program where a loan is  
 256:21 granted where the borrower simply states  
 256:22 where his or her income and assets are  
 256:23 and it's not verified, is that your  
 256:24 understanding?

257:1  
 257:2 A. Yes.  
 257:3 Q. And NINA would be a loan  
 257:4 program where the borrower doesn't even  
 257:5 have to say what his or her income and  
 257:6 assets are; is that right?

257:8 A. That's my understanding.  
 257:9 Q. And in this email near the  
 257:10 bottom of the first page Mr. Andrukonis  
 257:11 refers to NINA loans and says "I  
 257:12 recommend we pull out of this product  
 257:13 entirely if we can get the advocates to  
 257:14 support us."  
 257:15 Do you see that?  
 257:16 A. No. I'm sure it's here.  
 257:17 Q. Right near the bottom of the  
 257:18 first page. Do you see that?  
 257:19 A. Yes.

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257:23 A. Yes.

257:24 Q. And you remember having --  
257:25 what do you remember about your

258:2 discussions with Mr. Andrukonis about  
258:3 SISA and NINA loans?

258:5 A. I don't remember the  
258:6 specifics. He was generally concerned  
258:7 about them.

258:8 Q. Okay. Do you recall it being  
258:9 his view that Freddie Mac should not be  
258:10 purchasing NINA and SISA loans?

258:11 A. Not at the time I first talked  
258:12 to him about it.

258:13 Q. At some point was that his  
258:14 view as you understood it?

258:15 A. Yes.

258:16 Q. And did you agree with him on  
258:17 that?

258:19 A. We spent a lot of time talking  
258:20 about this with the people from different  
258:21 parts of the organization, and we had  
258:22 been doing these loans. So this is a  
258:23 question, you can see, the memo is sent  
258:24 in April 26th, I got there in January,  
258:25 right, so this was, you know, we have a

259:2 new guy should we stop doing these. And  
259:3 after spending a lot of time talking  
259:4 about it and getting different people's  
259:5 views in writing, we decided to stay in  
259:6 the market.

259:7 Q. And as CEO that was your  
259:8 decision to stay in that part of the  
259:9 market, right?

259:10 A. Well, it was a decision of the  
259:11 group as a whole, but I could have  
259:12 overridden the decision.

259:13 Q. But you didn't override it,

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259:14 you approved that decision, right?  
 259:15 A. Yes.  
 259:16 Q. Now, not too long after this  
 259:17 email Mr. Andrukonis was gone from  
 259:18 Freddie Mac; is that right?  
 259:19 A. Not too long after.  
 259:20 Q. Right. And what were the  
 259:21 circumstances of his departure?

259:23 A. Well, I think it was quite  
 259:24 awhile actually. It was a number of  
 259:25 months. Myself and Gene McQuade, who was

260:2 the chief operating officer, so it was  
 260:3 quite a few months before I hired him,  
 260:4 so, concluded that Dave as a member of  
 260:5 the senior executive team wasn't weighing  
 260:6 from both a broad mission standard,  
 260:7 mission perspective and shareholder  
 260:8 perspective all the varying  
 260:9 considerations we had to take while  
 260:10 making a loan, and that one of those  
 260:11 considerations was that, that we had to  
 260:12 be, we had to take all of these things  
 260:13 into consideration, not just credit  
 260:14 quality.

260:15 Q. What do you mean by all of  
 260:16 these things?

260:17 A. By all of these things I meant  
 260:18 liquidity, affordability, stability  
 260:19 mission objectives, our profitability  
 260:20 measures, and our fulfilling what the  
 260:21 Congress had mandated we had to do.

260:22 Q. Housing goals, in other words?

260:23 A. Well the Congress, no, the  
 260:24 Congress didn't -- the Congress didn't  
 260:25 just mandate housing goals, the Congress

261:2 mandated affordability, liquidity and  
 261:3 stability of the housing market.

261:4 Q. Is it accurate to say that Mr.  
 261:5 Andrukonis, he was fired, right?

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	<p>261:6 A. He resigned.</p> <p>261:7 Q. Well in fact --</p> <p>261:8 A. I believe.</p> <p>261:9 Q. He was asked to leave, right?</p> <p>261:11 A. I don't remember the exact</p> <p>261:12 specifics, but he -- we decided it wasn't</p> <p>261:13 mutually advantageous to continue.</p> <p>261:14 MR. STARK: I'll mark as the</p> <p>261:15 next exhibit a document with the</p> <p>261:16 first Bates number FHFA 08468679.</p> <p>261:17 (Syron Exhibit 34620 for</p> <p>261:18 identification, Bates stamped FHFA</p> <p>261:19 08468679 through 08468743.)</p> <p>261:20 Q. We've handed you, Mr. Syron, a</p> <p>261:21 document marked as Exhibit 34620, which</p> <p>261:22 is a transcript of your interview with</p> <p>261:23 the Financial Crisis Inquiry Commission</p> <p>261:24 on August 31, 2010. Do you see that?</p>
<b>Mudd Tr. at 209:25-211:15</b>	<p>209:25 Q The next exhibit is 35029. I think</p> <p>210:2 you'll recognize Exhibit 35029 as the transcript</p> <p>210:3 of your testimony before the Financial Crisis</p> <p>210:4 Inquiry Commission on April 9, 2010.</p> <p>210:5 Do you see that?</p> <p>210:6 A Yes.</p> <p>210:7 Q Do you recall that you testified before</p> <p>210:8 the Financial Crisis Inquiry Commission on or</p> <p>210:9 about April 9, 2010?</p> <p>210:10 A Yes.</p> <p>210:11 Q And in that testimony, did you testify</p> <p>210:12 under oath?</p> <p>210:13 A I assume so.</p> <p>210:14 Q And did you testify truthfully to the</p> <p>210:15 best of your ability?</p> <p>210:16 A Yes.</p> <p>210:17 Q If you could turn to page 71, please.</p> <p>210:18 And in the middle of the page there's a question</p> <p>210:19 from Commissioner Giorgio: Okay. All right. So</p> <p>210:20 really there were double -- there were at least</p> <p>210:21 two mandates that you were following here and a</p> <p>210:22 lot of your acquisitions of subprime and Alt-A</p>

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	<p>210:23 which was to -- was to increase your  210:24 profitability, increase your market share and  210:25 reach your housing goals -- reach your affordable</p> <p>211:2 housing goals. Would that be fair to say?  211:3 Mr. Levin says, Yes, sir. Commissioner  211:4 Giorgio says, Mr. Levin -- Mr. Mudd, rather,  211:5 you're nodding your head as well.  211:6 Mr. Mudd: I'm nodding my head because  211:7 I agree, yes.  211:8 Do you see that?  211:9 A Yes.  211:10 Q And was that truthful testimony?  211:11 A Yes.  211:12 Q And is this -- was it true of Fannie  211:13 Mae's purchases of PLS that they were made in part  211:14 to increase Fannie Mae's profitability?  211:15 A Yes, in part.</p>
<b>Mudd Tr. at 211:24-212:7</b>	<p>211:24 Q And were purchases of PLS made to meet  211:25 housing goals?</p> <p>212:2 A Yes, under the context that every --  212:3 that the loan count was on a loan-by-loan basis to  212:4 meet the housing goals, so every single loan that  212:5 you put on the books, whether it came through a  212:6 guarantee or portfolio or PLS counted towards  212:7 housing goals.</p>
<b>Niculescu Tr. at 104:12-105:17</b>	<p>104:12 Q. Do you recall that after these  104:13 calls or criticisms by Congress, that Fannie  104:14 Mae began to increase its purchases of  104:15 non-prime loans through private label  104:16 securities?</p> <p>104:18 A. Well, I don't remember when  104:19 these -- as we've said -- when these calls or  104:20 criticisms were voiced, so it's hard for me to  104:21 draw that connection.  104:22 I think, though, that you are  104:23 attempting to find a causal link between the  104:24 one and the other, and I'm not sure whether  104:25 that link exists or not. I would say that the</p>



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	<p>105:2 housing goals the company faced, which were  105:3 increasing each year, were goals that did have  105:4 an effect of causing the company to acquire  105:5 subprime private label securities and other  105:6 low FICO loans through its single-family  105:7 business, which it needed to do in order to  105:8 meet housing goals. So whether that was a  105:9 causal influence or another was a causal  105:10 influence, I really can't say.  105:11 Q. Do you recall that Fannie Mae  105:12 increased its purchases of private label  105:13 securities containing subprime and Alt-A loans  105:14 in 2005-2007?  105:15 A. I do recall that we increased  105:16 our purchases, but whether it was one year or  105:17 another I couldn't tell you at this point.</p>
<b>D. Cook Tr. at 278:18-280:16</b>	<p>278:18 Q Have you had a chance to take a look at  278:19 what's been marked as Exhibit 614?  278:20 A Yes.  278:21 Q Does this reflect that in pursuit of  278:22 increased purchases for subprime goals, Mr. Norris  278:23 listed ten items that Capital Markets should consider  278:24 that would alter their ordinary practices with respect  278:25 to PLS or other transactions?</p> <p>279:3 A As I read this, this only relates to housing  279:4 goals. It doesn't talk about the fact that to also  279:5 increase -- actually, I don't see anything -- does it  279:6 talk about housing goals here?  279:7 Q "Below is a list of possible exceptions that  279:8 we will need to increase our purchases for subprime  279:9 goals."  279:10 Do you understand that to be referring to  279:11 housing goals?  279:12 A Not necessarily.  279:13 Q What do you think "subprime goals" refers  279:14 to?  279:15 A This could have been a desire to invest in  279:16 more subprime collateral and, hence, get a larger  279:17 return. It could have been related to housing goals  279:18 also, but I don't read it that way.  279:19 Q Had you heard that there was a goal to</p>

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	<p>279:20 invest in more subprime?</p> <p>279:22 A I had heard, and I believe it might have  279:23 been in 2006, that Fannie Mae -- I hadn't heard this  279:24 goal specifically.</p> <p>279:25 Q You had not heard that there was a goal to</p> <p>280:2 purchase more subprime?</p> <p>280:3 A I hadn't heard this goal specifically as  280:4 it's referring to. I had heard, in this era of 2006,  280:5 and I'm not sure of the exact dates, there were goals  280:6 in Fannie Mae to increase subprime business, but  280:7 not -- not necessarily in PLS. I think that was in  280:8 our whole loan purchases.</p> <p>280:9 Q The individuals on this e-mail are on the  280:10 Capital Markets PLS side, correct?</p> <p>280:11 A Paul Norris was the director. Steve Shen  280:12 was his boss. And Ramon de Castro was his boss --  280:13 manager. And they all were related -- or worked in  280:14 PLS. Andrew Bon Salle was not directly related to  280:15 PLS. He was the SVP of Capital Markets Mortgage  280:16 Assets but not directly over PLS.</p>
<b>D. Cook Tr. at 394:13-18</b>	<p>394:13 In addition to housing goals, sir, was  394:14 providing liquidity to the secondary market for  394:15 mortgage and mortgage products one of the missions of  394:16 Fannie Mae?</p> <p>394:18 A Yes, as far as I understand.</p>
<b>Lockhart Tr. at 224:23-226:16</b>	<p>224:23 Q. The bottom paragraph, "The  224:24 decisions of the board of directors and  224:25 senior management prior to 2007 to acquire</p> <p>225:2 Alt-A loans and other high risk loan  225:3 products is a principal contributor to  225:4 Fannie Mae's current earnings losses and  225:5 deteriorated financial position. Members  225:6 of the executive management team made  225:7 imprudent decisions to increase market  225:8 share and enter into higher risk products  225:9 with outdated models and without all the  225:10 necessary information or reports to  225:11 evaluate the risks of its decisions."</p>

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	<p>225:12 Did that accurately reflect the 225:13 current state of Fannie Mae? 225:14 A. Yes. 225:15 Q. At that time. 225:16 And certainly by that time the 225:17 imprudent decisions that you were 225:18 referring to would have included decisions 225:19 to purchase private label securities? 225:20 A. Yes. 225:21 Q. Turn the page, 13, at the top, 225:22 the first full sentence says, "Senior 225:23 management and the board of directors made 225:24 these decisions to increase market share, 225:25 raise revenue and meet housing goals."</p> <p>226:2 Do you see that? 226:3 A. Yes.</p> <p>226:10 These would have included the 226:11 reasons for Fannie Mae's purchases of 226:12 private label securities during the '05 to 226:13 '07 time period, namely to increase market 226:14 share, raise revenue and meet housing 226:15 goals? 226:16 A. Yes.</p>
<b>Lockhart Tr. at 237:23-239:19</b>	<p>237:23 Q. Is that one? 237:24 A. They did it for the same 237:25 reasons, yes.</p> <p>238:2 Q. They were concerned about 238:3 competing with Fannie Mae? 238:4 A. Overall market share, but also 238:5 Fannie Mae, affordable housing goals and 238:6 profitability. 238:7 Q. Concerned about their relevance 238:8 in the marketplace?</p> <p>238:10 A. I don't think they were 238:11 concerned about their relevance in the 238:12 marketplace, they were, you know, they 238:13 were -- Fannie was a 900-pound gorilla 238:14 and they were a 700-pound gorilla, they</p>

<b>GSEs' Entry Into, and Participation in, the Subprime or Non-Traditional Loan Market</b>	
	<p>238:15 were relevant.  238:16 Q. A little further down there is  238:17 discussion of governance, "FHFA has  238:18 repeatedly raised concerns with the  238:19 critical weaknesses in board of directors  238:20 and management oversight and conduct. In  238:21 many instances, despite repeated warnings,  238:22 the board and management have failed to  238:23 correct the deficiencies. The  238:24 enterprises' boards and management have  238:25 failed to insure the safety and soundness</p> <p>239:2 of the enterprise, correct deficiencies  239:3 identified in ROEs, and other supervisory  239:4 correspondence and fully comply with the  239:5 2003 consent order. The director met with  239:6 the board of directors on several  239:7 occasions during the last year to discuss  239:8 these issues. Many of these and other  239:9 issues were discussed in the directors  239:10 monthly meetings with the chairman and the  239:11 board and chief executive officer, Richard  239:12 Syron."  239:13 Is that an accurate statement?  239:14 A. Yes.  239:15 Q. And you were the one who met  239:16 with the board of directors and Mr. Syron?  239:17 A. I met with the board of  239:18 directors and Mr. Syron; other members of  239:19 our team also did, but I did, yes.</p>
<b>Lockhart Tr. at 332:9-25</b>	<p>332:9 Q. I know you gave some testimony  332:10 earlier today on the subject of why did  332:11 the GSEs, Fannie Mae and Freddie Mac,  332:12 invest in PLS backed by Alt-A and subprime  332:13 mortgages.  332:14 A. Yes.  332:15 Q. I believe one of the principal  332:16 reasons was to meet affordable housing  332:17 goals set by HUD, is that right?  332:18 A. That was one of the three major  332:19 reasons; market share and profitability  332:20 were probably the other two, yes.</p>

<b>GSEs' Entry Into, and Participation in, the Subprime or Non-Traditional Loan Market</b>	
	<p>332:21 Q. So the three major reasons were</p> <p>332:22 satisfying affordable housing goals,</p> <p>332:23 achieving market share, and profitability,</p> <p>332:24 is that right?</p> <p>332:25 A. Yes.</p>
<b>Lockhart Tr. at 333:21-24</b>	<p>333:21 Q. On a profit point, is it</p> <p>333:22 accurate to say that Fannie Mae and</p> <p>333:23 Freddie Mac made more money on PLS</p> <p>333:24 investments than they would have made on</p> <p>333:25 other investments?</p> <p>334:3 A. Their major other investment</p> <p>334:4 was their own securities and certainly PLS</p> <p>334:5 had higher yields than their own</p> <p>334:6 securities.</p> <p>334:7 Q. Which is to say the return on</p> <p>334:8 their investment that they expected to get</p> <p>334:9 on PLS was better?</p> <p>334:10 A. They expected; obviously as it</p> <p>334:11 turned out, they did not get a return,</p> <p>334:12 but, yes, their expected return, yes.</p> <p>334:13 Q. In fact the GSEs, they really</p> <p>334:14 wanted to buy the PLS that they were</p> <p>334:15 buying, right?</p> <p>334:17 A. I am not sure what want means</p> <p>334:18 in this, but they needed to do it to meet</p> <p>334:19 their affordable housing goals and they</p> <p>334:20 certainly wanted the added profitability</p> <p>334:21 they expected from it.</p> <p>334:22 Q. And they also wanted to</p> <p>334:23 increase their market share?</p> <p>334:24 A. Right.</p>
<b>Lockhart Tr. at 236:18-238:15</b>	<p>236:18 Q. The criticisms of Freddie Mac</p> <p>236:19 were pretty similar, right, to the issues</p> <p>236:20 that were confronting Fannie Mae in the</p> <p>236:21 exhibit we just reviewed?</p> <p>236:22 A. That's correct.</p> <p>236:23 Q. Turn to page 6, first full</p> <p>236:24 paragraph says, "Examinations in 2005,</p> <p>236:25 2006, and 2007 highlighted the agency's</p>

<b>GSEs' Entry Into, and Participation in, the Subprime or Non-Traditional Loan Market</b>	
	<p>237:2 continuing concerns with the board's and  237:3 management's oversight and operation of  237:4 the enterprise, serious deficiencies in  237:5 credit risk management at a time when the  237:6 enterprise was acquiring riskier assets  237:7 and capital and liquidity plans which  237:8 could, in the event of market turmoil,  237:9 become stressed."  237:10           Was that an accurate depiction  237:11 of what was highlighted in the 2005, 2006,  237:12 and 2007 examinations?  237:13    A.   That's correct.  237:14    Q.   Freddie Mac purchased far more  237:15 private label securities than Fannie Mae,  237:16 right, during that same time period?  237:17    A.   Yes.  237:18    Q.   And Freddie Mac also purchased  237:19 private label securities for the same  237:20 reasons that Fannie Mae did, right, for  237:21 competitive reasons?</p> <p>237:23    Q.   Is that one?  237:24    A.   They did it for the same  237:25 reasons, yes.</p> <p>238:2    Q.   They were concerned about  238:3 competing with Fannie Mae?  238:4    A.   Overall market share, but also  238:5 Fannie Mae, affordable housing goals and  238:6 profitability.  238:7    Q.   Concerned about their relevance  238:8 in the marketplace?</p> <p>238:10   A.   I don't think they were  238:11 concerned about their relevance in the  238:12 marketplace, they were, you know, they  238:13 were -- Fannie was a 900-pound gorilla  238:14 and they were a 700-pound gorilla, they  238:15 were relevant.</p>
<b>Niculescu Tr. at at 126:9 to 127:2</b>	<p>126:9       Q.   Do you recall -- you testified  126:10 in the last segment that we looked at that  126:11 there was an explicit mandate to buy a certain</p>

<b>GSEs' Entry Into, and Participation in, the Subprime or Non-Traditional Loan Market</b>	
	<p>126:12 dollar volume of subprime loans; do you recall  126:13 we went over that?  126:14 A. Yes.  126:15 Q. What was that dollar volume; do  126:16 you recall?  126:17 A. No.  126:18 Q. But you do recall that in fact  126:19 Mr. Levin or others in senior management gave  126:20 an explicit mandate to buy a certain dollar  126:21 volume of subprime loans through PLS?</p> <p>126:23 A. I do recall the capital markets  126:24 division being instructed to buy a certain  126:25 dollar volume of private label securities</p> <p>127:2 backed by subprime, Alt-A loans.</p>
<b>Kain Tr. at 364:4-367:6</b>	<p>364:4 MR. BENNETT: Let's mark as our next  364:5 exhibit, a document Bates-numbered FHFA  364:6 01205065.  364:7 (Deposition Exhibit No. 20426 was  364:8 marked for identification.)  364:9 BY MR. BENNETT:  364:10 Q. It is 20426. Do you recognize  364:11 20426?  364:12 A. I recognize it now as an ICM all  364:13 staff meeting PowerPoint.  364:14 Q. Do you recall this ICM all staff  364:15 meeting in February of 2006?  364:16 A. I don't.  364:17 Q. Was it frequent -- was it a frequent  364:18 occurrence to have ICM all staff meetings?  364:19 A. I am guessing it was quarterly or  364:20 every six months or something like that.  364:21 Q. Do you believe you were a presenter  364:22 at this all staff meeting?  364:23 A. I probably was, yeah.  364:24 Q. In looking through this PowerPoint,  364:25 are you able to direct me to the parts that you</p> <p>365:2 may have presented?  365:3 A. I probably --</p>

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365:5 THE WITNESS: Sorry. In looking at  
365:6 it, there is a good chance I presented the  
365:7 mortgage investment structuring page, but I  
365:8 don't know that, you know, for a fact. But if  
365:9 I presented some part of this, it would most  
365:10 likely have been that page. I could have done  
365:11 other pages. It's possible.  
365:12 BY MR. BENNETT:  
365:13 Q. So if you go to that page, the  
365:14 mortgage investment structure page, I take it  
365:15 you are referring to Page 14?  
365:16 A. Yeah.  
365:17 Q. There is a heading: "Support GSE  
365:18 share in conforming market penetration  
365:19 objectives."  
365:20 What does that mean?  
365:21 A. In looking at it today, it appears  
365:22 to mean support Freddie Mac's share over Fannie  
365:23 GSE share and our overall penetration into the  
365:24 conforming market, which would mean other  
365:25 conforming loans that are going somewhere other  
  
366:2 than just the GSEs. That's the way I would  
366:3 interpret that.  
366:4 Q. So with respect to the GSE share, if  
366:5 you look at the second bullet, nonprime:  
366:6 "Achieve majority GSE share of nonprime  
366:7 mortgage market, 60 percent market share of  
366:8 Triple A rated subprime ABS."  
366:9 Do you see that?  
366:10 A. I see that.  
366:11 Q. Was it the goal of Freddie Mac in  
366:12 February of 2006 to achieve a 60 percent market  
366:13 share of Triple A rated subprime ABS with  
366:14 respect to its relationship with Fannie Mae?  
  
366:16 THE WITNESS: Again, you know, I  
366:17 don't remember that. In looking at it today,  
366:18 that appears to be a goal, but Fannie Mae --  
366:19 Fannie Mae was not able to purchase things in  
366:20 2005, and I don't know when that changed, so  
366:21 that may not have been very -- I don't know



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	<p>366:22 that that is a stretch number or it's not.  366:23 BY MR. BENNETT:  366:24 Q. And by stretch number, you mean a  366:25 number that would be --</p> <p>367:2 A. Easily hit or not easily hit. I  367:3 don't have any context to put that in, because  367:4 there were, you know, unique circumstances with  367:5 Fannie Mae, you know, and again, I'm looking at  367:6 it today.</p>
<b>Kain Tr. at 367:18-368:6 re</b>	<p>367:18 Q. In bold below that: "Increase Alt-A  367:19 market share and capabilities, purchase \$20  367:20 billion in whole loans."  367:21 What does that mean?  367:22 A. I think that relates to what we --  367:23 again, looking at it today, I think that  367:24 relates to what we talked about earlier where  367:25 the portfolio and the guarantee business would</p> <p>368:2 bid together, and the hope was that that would  368:3 allow us to buy more Alt-A loans even if we  368:4 didn't have the best bid for credit. So that  368:5 was an example. And again, you know, so that  368:6 is the way I interpret that.</p>
<b>Aneiro Tr. at 54:16-23</b>	<p>54:16 Q. Setting aside your  54:17 expectation, was it your experience that  54:18 Freddie Mac's volume of purchases in the  54:19 AAA private label securitization space  54:20 did in fact increase in 2005, 2006  54:21 relative to the prior years that you'd  54:22 been at Freddie Mac?  54:23 A. Yes.</p>
<b>Kenneweg 30(b)(6) Tr. at 76:17-24</b>	<p>76:17 Q. Let me ask you to take a look,  76:18 Ms. Kenneweg, at Exhibit 1827. This appears  76:19 to be an operational review from AMO on  76:20 ResMAE. Do you see that?  76:21 A. Yes.  76:22 Q. Do you understand ResMAE to be  76:23 a loan originator?  76:24 A. I do.</p>
<b>Kain Tr. at 476:4-13</b>	<p>476:4 Do you remember it being the case in  476:5 early 2007 that Freddie Mac was concerned about</p>

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	476:6	falling short of its long-term returns or
	476:7	long-term returns?
	476:8	A. I don't remember that specific --
	476:9	you know, that specific time period and
	476:10	discussion. I think there were many times in
	476:11	Freddie Mac's history where it was concerned
	476:12	about, you know, not being able to meet its
	476:13	kind of desired returns.
<b>Romano Tr. at 239:11-240:17</b>	239:11	Q. Freddie Mac's understanding of what
	239:12	the products and practices in the mortgage
	239:13	business at the time in your view, would have
	239:14	been as good as or better than anyone else's?
	239:16	MR. OBLAK: Join.
	239:17	THE WITNESS: I believe Freddie
	239:18	Mac's experience in the mortgage business is
	239:19	they have tremendous insight and information
	239:20	into the mortgage default probability of the
	239:21	loans that contain risk characteristics such as
	239:22	these or other loans.
	239:23	BY MR. BREBNER:
	239:24	Q. And Freddie Mac's tremendous insight
	239:25	into the mortgage business would have been in
	240:2	your view as good as or better than other
	240:3	market participants?
	240:5	MR. MORVILLO: Join.
	240:6	THE WITNESS: I believe Freddie Mac
	240:7	has a long track record and has the information
	240:8	and I think it is pretty good.
	240:9	BY MR. BREBNER:
	240:10	Q. In the 2005 to 2007 time period,
	240:11	that would have been true?
	240:13	THE WITNESS: Freddie Mac had
	240:14	information in 2005 through 2007 that was very
	240:15	instructive for understanding risk, but there
	240:16	were still risks that were going on that not
	240:17	even Freddie Mac had experienced in the past.
<b>Romano Tr. at 385:4 to 386:8</b>	385:4	Q. -- at the time you proposed that
	385:5	conversation?

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	<p>385:6 A. I believe there was a real 385:7 possibility that we were passed the point of 385:8 reasonableness, yes.</p> <p>385:9 Q. And you were past the point of 385:10 reasonableness not simply with respect to 385:11 lending to investors, but also more generally 385:12 with respect to some of the origination 385:13 practices in the marketplace that you were 385:14 concerned about?</p> <p>385:16 THE WITNESS: This was specific to 385:17 investors. I would think my concerns relative 385:18 to market practices for untested products has 385:19 been outlined and articulated in the documents 385:20 you -- you've actually presented here.</p> <p>385:21 BY MR. BREBNER:</p> <p>385:22 Q. And your concerns with the practices 385:23 with respect to untested products in the 2005 385:24 time period were such that -- that you believed 385:25 that Freddie Mac should be getting out of</p> <p>386:1 RAYMOND ROMANO 386:2 those, correct?</p> <p>386:4 THE WITNESS: My view of those 386:5 practices were that they were untested. We 386:6 didn't have any sufficient experience in it. 386:7 We should limit the amount of exposure we took 386:8 to those products.</p>
<b>Syron Tr. at 129:14 to 130:12</b>	<p>129:14 Q. And it says here, "As long as 129:15 some institutions operate under 129:16 different, or no, regulatory strictures, 129:17 potential for these sorts of excesses and 129:18 abuses will exist. As previously stated, 129:19 Freddie Mac has a long history of 129:20 voluntarily setting standards of prudent 129:21 underwriting and of promoting greater 129:22 borrower protections in subprime."</p> <p>129:23 Do you see that?</p> <p>129:24 A. Yes.</p> <p>129:25 Q. And was that a true statement?</p> <p>130:2 A. Yes.</p>

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130:3 Q. When you referred to prudent  
130:4 underwriting, can you describe what you  
130:5 meant there?

130:6 A. Prudent underwriting would  
130:7 mean that it was not predatory.

130:8 Q. What do you mean by not  
130:9 predatory?

130:10 A. That in fact we expected the  
130:11 person who took the loan would be able to  
130:12 service it.

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<b>Romano Tr. at 235:14-24</b>	<p>235:14 Q. When you had concerns about untested  235:15 mortgage products in the time period 2005 to  235:16 2007, your concerns about those untested  235:17 products were in part because Freddie wasn't  235:18 able to fully and accurately model the default  235:19 risk, correct?</p> <p>235:21 THE WITNESS: I believe my concerns  235:22 were that we would not be able to model the  235:23 default risk in both expected and unexpected  235:24 events.</p>
<b>Vetrano Tr. at 293:12-294:10</b>	<p>293:12 A. I see that.  293:13 Q. And then the paragraph below  293:14 that reads, "Even if we obtained the most  293:15 recent DEFCAP version, views on Alt-A are  293:16 changing almost daily. Although we need a  293:17 more recent read than June 2005, it almost  293:18 doesn't make sense to develop a 'final' Alt-A  293:19 matrix until the dust clears and a consistent  293:20 corporate view of Alt-A risk emerges."  293:21 Do you see that?  293:22 A. I see that.  293:23 Q. At this time were there  293:24 different views within Freddie Mac about the  293:25 risks of Alt-A loans?</p> <p>294:2 A. Freddie Mac's DEFCAP model was  294:3 developed based on 30 years of history. Any  294:4 time we had less than 30 years of history  294:5 there was debate.  294:6 Q. At this time do you recall  294:7 debate about the risks of Alt-A loans?  294:8 A. I remember debates about all  294:9 mortgage products for which we had less than  294:10 30 years of data.</p>
<b>Vetrano Tr. at 422:17-429:15</b>	<p>422:17 Q. The sentence then goes on to  422:18 say: "We need to remain wary of blind spots  422:19 in our models."  422:20 Do you see that?  422:21 A. I see that.  422:22 Q. Do you know what you mean by  422:23 "blind spots" in your models?</p>

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422:24 A. I don't recall the context  
422:25 within which this was written.

423:2 Q. Okay. Regardless of whether  
423:3 you recall the context in which this is  
423:4 written, is it fair to say that a blind spot  
423:5 in a model is a place in the model where  
423:6 you're making assumptions or making decisions,  
423:7 but you don't know information that might  
423:8 exist out in the real world?

423:10 A. That's a possible result.

423:11 Q. Is there any other definition  
423:12 of a blind spot in the model that you would  
423:13 have, sitting here today?

423:15 A. As we did discuss yesterday,  
423:16 the DEFCAP model was designed around 30 or 40  
423:17 years of data, and we were using best  
423:18 information available for this purpose for  
423:19 which we did not have 30 or 40 years of data.  
423:20 I would guess that one possibility is a  
423:21 recognition that we did not have 30 or 40  
423:22 years of data for this model, and therefore  
423:23 needed to be cautious about what the results  
423:24 said.

423:25 Q. You said that DEFCAP used 30 to

424:2 40 years of data. Do you know what 30 to 40  
424:3 years it looked at?

424:4 A. Freddie Mac's history of  
424:5 single-family 30-year, 15-year data, is what  
424:6 the model was honed on.

424:7 Q. Sorry. When you say 30-year  
424:8 and 15-year data, those sound to me like  
424:9 durations of mortgages. Is that -- are you  
424:10 saying that you based the DEFCAP model on  
424:11 Freddie Mac's experience with 30-year mortgage  
424:12 products?

424:14 A. The original use of the DEFCAP  
424:15 model was to evaluate the risk of its generic  
424:16 business, which was comprised primarily of

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424:17 30-year fixed-rate mortgages and 15-year  
424:18 fixed-rate mortgages. The calibrations of the  
424:19 model incorporated experience from as far back  
424:20 as Freddie Mac's data goes, and I am not sure  
424:21 how far it goes back, hence my 30 to 40 years.  
424:22 I am guessing. And that was the origins and  
424:23 the primary use of the model.

424:24 Q. Do you know whether any of the  
424:25 data used went -- in order to calibrate the

425:2 DEFCAP model, preceded the year 1970?

425:3 A. I do not know.

425:4 Q. If you turn in the document I  
425:5 have just shown you to the page Bates-numbered  
425:6 ending in 4651. The paragraph number 3, the  
425:7 last sentence there says: "For AAA risk, we  
425:8 want reasonable assurance that the credit  
425:9 enhancement will protect our bond principal  
425:10 even in the most disastrous economic  
425:11 scenario."

425:12 Do you see that?

425:13 A. I do see that.

425:14 Q. Do you know what was assumed in  
425:15 the model as the most disastrous economic  
425:16 scenario?

425:18 A. I do not.

425:19 Q. Do you know if you knew at the  
425:20 time what was assumed in the model as the  
425:21 disastrous economic scenario?

425:22 A. I do not.

425:23 Q. How did you develop any  
425:24 reasonable assurance then that the credit  
425:25 enhancement would protect the bond principal

426:2 even in the most disastrous economic scenario?

426:5 A. I don't recall writing this  
426:6 memo, but the third paragraph, second  
426:7 sentence, perhaps provides some guidance to  
426:8 that question.

426:9 Q. Sir, could you read it?

426:10 A. I'll read the sentence

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426:11 preceding it also.

426:12 Q. Sure.

426:13 A. "Another approach would make  
426:14 use of loss distributions, a direct credit  
426:15 analogy to the use of multiple prepay paths in  
426:16 OAS models. This is the concept behind 300  
426:17 credit paths generated by DEFCAP. The least  
426:18 probable extremes (e.g., 99th or 100th  
426:19 percentile) could define a minimum by which  
426:20 AAA credit enhancements could be compared,  
426:21 similar to the '4 times' rule."

426:22 Q. Okay. And so can you tell me  
426:23 then how that ensures that you will have  
426:24 reasonable assurance that the credit  
426:25 enhancement will protect the bond principal

427:2 even in the most disastrous economic  
427:3 circumstances?

427:5 A. The 300th path, which is  
427:6 randomly generated, which is why I could not  
427:7 tell you what the worst scenario is,  
427:8 represents the worst combination of interest  
427:9 rate and credit scenarios out of 300. Nothing  
427:10 is ensured, nothing is certain, but it  
427:11 provides -- again, my reading as I sit here  
427:12 today -- a reasonable comparison to a set of  
427:13 metrics developed by what was considered at  
427:14 that time another smart set of experts who  
427:15 worked with this concept.

427:16 Q. And so the 300 credit paths you  
427:17 said was randomly developed, and this refers  
427:18 to this model being similar to the prepay  
427:19 paths in the OAS models, correct?

427:20 A. That is what it says.

427:21 Q. And I believe you testified  
427:22 yesterday that the OAS models you were working  
427:23 on used Monte Carlo simulations?

427:24 A. That's correct.

427:25 Q. And so these 300 paths are

428:2 essentially generated by Monte Carlo  
428:3 simulations, is that right?



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	<p>428:4 A. That is correct.</p> <p>428:5 Q. When the computer generates the</p> <p>428:6 Monte Carlo simulations, what data does it use</p> <p>428:7 to determine the range of possible economic</p> <p>428:8 effects or interest rates or credit?</p> <p>428:10 A. I don't recall.</p> <p>428:11 Q. Did you know at the time?</p> <p>428:12 A. Conceptually.</p> <p>428:13 Q. Well, what did you know</p> <p>428:14 conceptually at the time?</p> <p>428:15 A. That part of looking back 30</p> <p>428:16 and 40 years is understanding what the</p> <p>428:17 volatility of interest rates were over that</p> <p>428:18 time, what the volatility of house price</p> <p>428:19 inflation was over that time, and based on</p> <p>428:20 past volatilities as an input, and I don't</p> <p>428:21 know what other inputs were put into the</p> <p>428:22 model, that an expected volatility would be</p> <p>428:23 one of the outputs.</p> <p>428:24 Q. So if I understand that</p> <p>428:25 correctly, then, the data that was put in to</p> <p>429:2 set the range of potential outputs was based</p> <p>429:3 on historical experience in terms of</p> <p>429:4 volatility, is that right?</p> <p>429:6 A. That is my guess.</p> <p>429:7 Q. And if an economic scenario</p> <p>429:8 happened that was worse than any historical</p> <p>429:9 experience that the model had used to generate</p> <p>429:10 these volatility ranges, the model may not be</p> <p>429:11 able to accurately predict the losses that</p> <p>429:12 would be suffered, is that fair?</p> <p>429:14 A. What you have described is</p> <p>429:15 always true, with any model.</p>
<p><b>Lockhart Tr. at</b>  <b>324:22-330:19</b></p>	<p>324:22 Q. But certainly by the first half</p> <p>324:23 of 2007 credit quality in that sector was</p> <p>324:24 rapidly deteriorating, is that right?</p> <p>324:25 A. Yes; although, again, that</p> <p>325:2 rapid there would not compare to anything</p>

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325:3 that happened later.  
 325:4 Q. It got more rapid?  
 325:5 A. Yes.  
 325:6 Q. And that deterioration, as it  
 325:7 says here, was widely reported, is that  
 325:8 right?  
 325:9 A. Yes.  
 325:10 Q. So folks at OFHEO and Fannie  
 325:11 Mae and Freddie Mac were all aware of that  
 325:12 deterioration in the time frame of the  
 325:13 first half of 2007, right?  
 325:14 A. Yes.  
 325:15 Q. I would like to turn back to  
 325:16 page 7, if you would, still in Exhibit  
 325:17 35919.  
 325:18 There is a section on page 7  
 325:19 that refers to models and you said Fannie  
 325:20 Mae, do you see that?  
 325:21 A. Yes.  
 325:22 Q. The second paragraph under that  
 325:23 heading says "Models are less dependable  
 325:24 and require adjustment when the economic  
 325:25 environment is outside of historical  
  
 326:2 experience," do you see that?  
 326:3 A. Yes.  
 326:4 Q. In the first half of 2007, was  
 326:5 the economic environment becoming outside  
 326:6 of historical experience?  
 326:7 A. I can't necessarily say that; I  
 326:8 don't know, I mean, again, I said we had  
 326:9 the Texas oil patch and California and I  
 326:10 think housing prices actually in the first  
 326:11 part of 2007 hadn't deteriorated as badly  
 326:12 as some of those examples, it took longer  
 326:13 than the first half of 2007.  
 326:14 Q. Ultimately did we in this  
 326:15 country experience an economic environment  
 326:16 that was outside of historical experience?  
 326:17 A. Most definitely.  
 326:18 Q. It goes on to say "Models are  
 326:19 estimated using selected historical  
 326:20 experience as a guide when circumstances

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326:21 are such that no historical experience can  
 326:22 provide insight for model builders, models  
 326:23 are very unlikely to produce accurate  
 326:24 projections."

326:25 Do you see that?

327:2 A. Yes.

327:3 Q. Did that become true of the  
 327:4 models that Fannie Mae and Freddie Mac  
 327:5 were using?

327:6 A. Yes.

327:8 Q. Did that issue affect others in  
 327:9 the mortgage industry, as far as you know?

327:11 A. Pretty much everybody that held  
 327:12 mortgages during the 2007, 2008, 2009  
 327:13 period had massive losses, so, yes.

327:14 Q. And that would include the  
 327:15 issuers and dealers in private label  
 327:16 securities backed by Alt-A and subprime  
 327:17 mortgages, would it not?

327:19 A. I don't know what their  
 327:20 portfolios were like, what they held and  
 327:21 what they sold.

327:22 But certainly if they held  
 327:23 private label mortgage-backed securities,  
 327:24 they would have been hurt; if they held  
 327:25 Fannies and Freddie's, they would not have

328:2 been hurt.

328:3 Q. If you turn over to page 9 in  
 328:4 35919, first full paragraph at the top of  
 328:5 the page says that, "Mortgage market  
 328:6 turmoil has resulted in a significant  
 328:7 increase in the model risk within market  
 328:8 risk models. Prepay models are challenged  
 328:9 by the sudden deterioration in mortgage  
 328:10 credit markets and falling home prices."

328:11 Do you see that?

328:12 A. Yes.

328:13 Q. Was that an accurate statement

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328:14 at the time of an issue that Fannie Mae  
 328:15 and Freddie Mac were facing?  
 328:16 A. Yes; I mean, this is an  
 328:17 interest rate risk issue, not a credit  
 328:18 risk issue, and because of what was going  
 328:19 on, it was very hard to understand when  
 328:20 people might prepay or one way to prepay  
 328:21 is actually being foreclosed on.  
 328:22 So that was going on and  
 328:23 messed up the models as well.  
 328:24 MR. STARK: I would like to  
 328:25 mark the next exhibit.

329:2 This will be Exhibit 35920.  
 329:3 ( Exhibit 35920, letter dated  
 329:4 September 4, 2008, was marked for  
 329:5 identification, as of this date.)  
 329:6 Q. Do you recognize Exhibit 35920?  
 329:7 A. Yes, this is a letter sent to  
 329:8 Freddie that was similar to the one we  
 329:9 just talked about at Fannie.  
 329:10 Q. This is a letter dated  
 329:11 September 4, 2008, correct?  
 329:12 A. Yes, the letter is dated that.  
 329:13 Q. It is similar to 35919, this  
 329:14 was signed by Mr. Dickerson, but you  
 329:15 reviewed and approved this, right?  
 329:16 A. Yes, and as you can see, it is  
 329:17 a draft letter and the idea was that the  
 329:18 CEOs would have a chance to respond to it.  
 329:19 Obviously events happened such  
 329:20 that they never responded.  
 329:21 MR. COREY: And this also came  
 329:22 from the FCIC website?  
 329:23 MR. STARK: Yes.  
 329:24 Q. Would it be accurate to say  
 329:25 this letter is rather similar to the

330:2 letter that went to Fannie Mae?  
 330:3 A. Very similar, yes.  
 330:4 Q. And raised similar concerns?  
 330:5 A. Yes.  
 330:6 Q. And includes the finding by

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	<p>330:7 FHFA that Freddie Mac had been engaged in  330:8 unsafe and unsound practices, right?  330:9 A. Yes.  330:10 Q. In particular, Freddie Mac, as  330:11 with Fannie Mae, had been engaged in  330:12 unsafe and unsound practices in relation  330:13 to Alt-A and subprime mortgages throughout  330:14 the period 2006, 2007, correct?</p> <p>330:16 A. Yes; I mean, both enterprises  330:17 took on more risk and certainly as the  330:18 market deteriorated, it was showing up in  330:19 the results.</p>
<b>P. Cook Tr. at  144:12-147:2</b>	<p>144:12 Q Okay. The first part of that paragraph  144:13 reads, Another dimension of risk to consider is  144:14 underwriting risk and process risk. Freddie Mac  144:15 policies are designed to prevent us from taking on  144:16 unacceptable layers of risk, example, thresholds  144:17 on LTV and FICO. However, how can we ensure that  144:18 a lender's property assessment process is, in  144:19 fact, providing us with LTVs we're comfortable  144:20 with?</p> <p>144:21 Do you see that?</p> <p>144:22 A Yes.</p> <p>144:23 Q What's "LTV" as it's used there?</p> <p>144:24 A Loan to value.</p> <p>144:25 Q And was there a concern about ensuring</p> <p>145:2 that a lender's property assessment process is  145:3 providing Freddie Mac with LTVs that it was  145:4 comfortable with?</p> <p>145:6 THE WITNESS: So this paragraph and  145:7 this discussion relates to the single family  145:8 business, and LTVs are important to Freddie Mac  145:9 because by charter we are able to ensure up to  145:10 80 percent of a loan's property without needing  145:11 mortgage insurance.</p> <p>145:12 So, yes, LTVs and, therefore, the  145:13 associated valuation models are important to  145:14 Freddie Mac in that underwriting.</p> <p>145:15 BY MR. FRANKEL:</p> <p>145:16 Q And was there some concern that based</p>

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	<p>145:17 on the lender's property assessment process  145:18 that -- that you might not be able to trust the  145:19 accuracy of LTVs that were being represented to  145:20 you?</p> <p>145:22 THE WITNESS: Actually, I think the  145:23 issue is well-described in the first sentence of  145:24 the prior paragraph where it says, Unlike the past  145:25 few years of rising house prices across most of</p> <p>146:2 the country, there has been more regional  146:3 volatility in house prices recently. And I think  146:4 that dynamic created less certainty around the  146:5 appraisal process than you might have had in prior  146:6 periods.</p> <p>146:7 BY MR. FRANKEL:  146:8 Q And how did the appraisal process  146:9 relate to the LTV -- LTV value?  146:10 LTV is based on an appraisal; right?  146:11 A Yes.  146:12 Q So if the -- if an appraisal was  146:13 unreliable or inaccurate, then the LTV would  146:14 necessarily be unreliable or inaccurate; right?</p> <p>146:17 THE WITNESS: Given the volatility in  146:18 house prices, it was more difficult to assess a  146:19 property value than it had been in the past.</p> <p>146:20 BY MR. FRANKEL:  146:21 Q And why was that a concern to Freddie  146:22 Mac?</p> <p>146:24 THE WITNESS: It would be a concern to  146:25 any lender because you're determining the amount</p> <p>147:2 of the loan based on that appraisal value.</p>
<p><b>Niculescu Tr. at  204:7-208:21</b></p>	<p>204:7 Q. Let me hand you what's been  204:8 marked as Exhibit 35807, if I might.  204:9 ---  204:10 (Exhibit 35807, e-mail chain,  204:11 topmost e-mail dated September 18, 2006, from  204:12 Chuck Greener to Peter Niculescu, Bates  204:13 FHFA01260329 through 332 was marked for  204:14 identification)</p>

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204:15 ---  
 204:16 BY MR. BLATT:  
 204:17 Q. Do you see that this is a copy  
 204:18 of an article that Otto Schultz sent to you on  
 204:19 September 18, 2006 and that you then forwarded  
 204:20 on to Chuck Greener, the article being  
 204:21 entitled "Fannie Mae Could Be Hit Hard By  
 204:22 Housing Bust"; do you see that?  
 204:23 A. Yes.  
 204:24 Q. Do you recall receiving this  
 204:25 article, and forwarding it on?

205:2 A. Let me have a look at it.  
 205:3 Q. Absolutely.  
 205:4 ---  
 205:5 (Witness reviewing document.)  
 205:6 ---  
 205:7 A. Yes?  
 205:8 Q. My question is: Do you recall  
 205:9 receiving and forwarding this on?  
 205:10 A. No.  
 205:11 Q. Okay. I would like to look at  
 205:12 page 331. It's the second page of the  
 205:13 article, the third page of the exhibit.  
 205:14 A. Yes.  
 205:15 Q. In the middle there is a  
 205:16 paragraph or a sentence that begins: "If a  
 205:17 housing slowdown causes subprime foreclosure  
 205:18 loss rates..."  
 205:19 Do you see that?  
 205:20 A. No.  
 205:21 Q. It's about halfway down.  
 205:22 A. On 331?  
 205:23 Q. Yes. "If a housing slowdown  
 205:24 causes subprime" --  
 205:25 A. Oh, yes.

206:2 MR. COREY: Right in the middle  
 206:3 of the paragraph.  
 206:4 A. Yes.  
 206:5 Q. So there is a line in here that  
 206:6 states: "If a housing slowdown causes  
 206:7 subprime foreclosure loss rates to rise to

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206:8 between 6 and 8%, Fannie could lose \$22  
 206:9 billion to \$29 billion, Berg estimated in his  
 206:10 letter. That's more than half of the roughly  
 206:11 \$40 billion in capital that Fannie had at the  
 206:12 end of March, according to OFHEO. Foreclosure  
 206:13 loss rates on subprime mortgages are currently  
 206:14 lower than Berg's theoretical range, but some  
 206:15 experts are worried that foreclosure could  
 206:16 increase in coming years. 'There is a high  
 206:17 probability of a sharp increase in credit  
 206:18 losses in the second half of 2007 and into  
 206:19 2008,' said Robert Lacoursiere, an analyst at  
 206:20 Banc of America Securities. 'This will be  
 206:21 more pronounced in subprime and will hit  
 206:22 earlier in that area, too.'

206:23 Do you see that?

206:24 A. Yes.

206:25 Q. Did you disagree in 2006 that

207:2 there was a high probability of a sharp  
 207:3 increase in credit losses on subprime loans in  
 207:4 2007?

207:6 A. I think your question is not  
 207:7 specifically with reference to the numbers in  
 207:8 this article. Is that correct?

207:9 Q. No, I'm just asking about first  
 207:10 the prediction by the Banc of America  
 207:11 Securities analyst that there is a "high  
 207:12 probability of a sharp increase in credit  
 207:13 losses in the second half of 2007."

207:14 And my question -- and he  
 207:15 specifically then says it will be "more  
 207:16 pronounced in subprime," and it will actually  
 207:17 "hit earlier in that area, too."

207:18 My question is; did you agree  
 207:19 or disagree with that analysis by the Banc of  
 207:20 America analyst?

207:21 A. I don't remember the analysis  
 207:22 by the Banc of America analyst. If your  
 207:23 question is more general, I could answer it,  
 207:24 but this particular analysis, I don't  
 207:25 remember.



<b>Risk of Subprime Loans and Other Non-Traditional Loan Products</b>	
	<p>208:2 Q. Did you appreciate in 2006 that</p> <p>208:3 there was a high probability of an increase in</p> <p>208:4 credit losses on subprime loans going forward?</p> <p>208:6 A. Well, insofar as home prices</p> <p>208:7 had been appreciating up through some time in</p> <p>208:8 2006, and at that point flattened out or</p> <p>208:9 started to drop, it would be a matter of</p> <p>208:10 course that you would expect an increase in</p> <p>208:11 credit losses going forward from what had been</p> <p>208:12 extraordinarily low levels previously. And</p> <p>208:13 the areas in mortgage credit that were most</p> <p>208:14 sensitive were the areas with high LTV or low</p> <p>208:15 credit scores, which tended to be more</p> <p>208:16 pronounced in subprime than in the prime</p> <p>208:17 areas.</p> <p>208:18 Having said that, these are</p> <p>208:19 simply matters of common record and common</p> <p>208:20 sense. I can't comment on the specific</p> <p>208:21 analysis.</p>
<b>Salahuddin Tr. at 352:14-24</b>	<p>352:14 Q. Were you aware that Fannie Mae</p> <p>352:15 purchased PLS containing loans that had</p> <p>352:16 credit risk layering?</p> <p>352:18 A. I'm aware that Fannie Mae</p> <p>352:19 purchased private label securities that</p> <p>352:20 had loans with layered credit risk, but</p> <p>352:21 at the time I was also aware that all of</p> <p>352:22 those loans were originated within the</p> <p>352:23 guidelines that the originator, within</p> <p>352:24 the originator's guidelines.</p>
<b>Niculescu Tr. at 41:15-43:3</b>	<p>41:15 Q. Okay. What risks did Fannie</p> <p>41:16 Mae's purchase of subprime and Alt-A private</p> <p>41:17 label securities pose to Fannie Mae?</p> <p>41:19 A. The -- I believe that at the</p> <p>41:20 time that the purchases were made the obvious</p> <p>41:21 risks were those of credit for the underlying</p> <p>41:22 securities, although we believed at the time</p> <p>41:23 that that credit risk was very substantially</p> <p>41:24 mitigated by the subordination and credit</p> <p>41:25 enhancement of those securities.</p>

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	<p>42:2           And I suppose also there was a  42:3 risk that the company would deploy capital in  42:4 a form that presented a reasonable -- what  42:5 appeared to be at the time a reasonable  42:6 expected return, but that conceivably other  42:7 opportunities for higher returns might become  42:8 available later and might not be available to  42:9 the company as a result of its investments in  42:10 these securities.</p> <p>42:11           It subsequently turned out, I  42:12 want to acknowledge, that the market pricing  42:13 of the securities purchased dropped very  42:14 substantially, which ultimately resulted in a  42:15 significant loss to capital for the company.  42:16 It was not anticipated at the time of the  42:17 purchases.</p> <p>42:18           Q.   What's credit risk?</p> <p>42:19           A.   I think that a common  42:20 definition would be a loss in an investment  42:21 that arises as a result of declines in the  42:22 credit or creditworthiness of the individuals  42:23 or institutions that are paying the loans, or  42:24 that have the loans.</p> <p>42:25           Q.   So does it include the risk</p> <p>43:2 that a borrower won't make mortgage payments?</p> <p>43:3           A.   Yes.</p>
<b>Niculescu Tr. at  43:25-44:9</b>	<p>43:25           Q.   If enough borrowers on loans</p> <p>44:2 underlying a private label security that  44:3 Fannie Mae bought failed to make mortgage  44:4 payments, can that result in Fannie Mae  44:5 incurring a loss?</p> <p>44:6           A.   Yes, it could.</p> <p>44:7           Q.   And did Fannie Mae understand  44:8 that when purchasing private label securities?</p> <p>44:9           A.   Yes, they did.</p>
<b>D. Cook Tr. at  80:2-7</b>	<p>80:2    A   The participants in the PLAT, including Risk  80:3 Management -- when I say Risk Management, Risk  80:4 Oversight -- including the Capital Markets Mortgage  80:5 Asset Management, all parties felt it would be  80:6 prudent, where possible, to add additional risk</p>

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	80:7 management functions to the process.
<b>D. Cook Tr. at 80:14-81:3</b>	<p>80:14 You said that the participants in the PLAT  80:15 "felt it would be prudent, where possible, to add  80:16 additional risk management functions to the process."  80:17 And I'm asking you that they deemed it prudent to do  80:18 so because the members of the PLAT were having an  80:19 increasing awareness of the risks inherent in private  80:20 label securities, correct?</p> <p>80:22 A I wouldn't say they were having an  80:23 increasing awareness. I would say people at Fannie  80:24 Mae, from when I was involved in 2004, they were  80:25 always aware of the risk and -- but the thinking</p> <p>81:2 evolved over time that it would be prudent to add a  81:3 function presettlement and precommitment.</p>
<b>D. Cook Tr. at 132:19-133:22</b>	<p>132:19 Q Did that group conduct analysis to evaluate  132:20 whether PLS it were -- it was purchasing was backed by  132:21 loans that were likely to perform, by which I mean for  132:22 which the mortgagees were going to actually pay their  132:23 mortgage?</p> <p>132:25 A So PLS have credit risk. There's risk</p> <p>133:2 from -- from the loan -- from the loans not paying,  133:3 but there's also structure, and there's subordination  133:4 and --</p> <p>133:5 Q Sure.</p> <p>133:6 A So analyzing a PLS, it wasn't just about  133:7 analyzing the collateral, but analyzing the structure  133:8 and the rating agency rating of the bonds.</p> <p>133:9 Q Okay. Did the Portfolio Transactions group  133:10 analyze credit risk?</p> <p>133:12 A Yes.</p> <p>133:13 Q And did the Portfolio Transactions group  133:14 also analyze structure risk?</p> <p>133:15 A Yes.</p> <p>133:17 Q And did I understand you to say that they  133:18 also analyzed subordination risk or enhancement risk?</p>

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	<p>133:19 Is that correct?</p> <p>133:21 A Yes, they analyzed those risks during their 133:22 assessment of the value of the deals.</p>
<b>D. Cook Tr. at 237:6-14</b>	<p>237:6 Q Mr. Cook, before we took a break, we were 237:7 still on that 2006 PLS risk policy. I'm sure you rue 237:8 the day that you wrote it. And we were talking about 237:9 section 5.1. The question that I had asked was 237:10 whether the risks that are listed in section 5.1 are 237:11 an accurate -- is an accurate list of the risks that 237:12 Fannie Mae was concerned with managing with respect to 237:13 PLS. 237:14 A Yes.</p>
<b>D. Cook Tr. at 240:2-240:9</b>	<p>240:2 In assessing or monitoring the risk, and, 240:3 specifically, the credit risk associated with PLS, did 240:4 Fannie Mae analyze loan level characteristics?</p> <p>240:6 A To the extent that loan level information 240:7 was provided to any investor in a PLS, Fannie Mae 240:8 would use that loan level information in -- in the 240:9 process of its risk assessment of the bonds</p>
<b>D. Cook Tr. at 326:20-327:11</b>	<p>326:20 Q Continuing into the "Next Steps" bullets, 326:21 the third of those reads, "Despite the authority 326:22 granted to the RPC, the size, strategic importance, 326:23 and risks of this portfolio (see risk summary in 326:24 attachment B) have caused me to conclude that the 326:25 strategy and any resulting limit changes be approved</p> <p>327:2 at a level more senior than the risk policy committee, 327:3 RPC." 327:4 Is that correct? 327:5 A Yes. 327:6 Q Did Fannie view the size, strategic 327:7 importance, and risks of the PLS portfolio as 327:8 warranting an approval of any increase at a level more 327:9 senior than the RPC?</p> <p>327:11 A I think Adolfo Marzol concluded that.</p>
<b>D. Cook Tr. at 337:6-17</b>	<p>337:6 Q Is it correct that the position limit with 337:7 respect to the PLS portfolio at Fannie Mae reflected 337:8 particular concern about the risks associated with 337:9 that portfolio?</p>

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	<p>337:11 A Risk may have been part of the reason for</p> <p>337:12 the position limit. I'm not sure it was the only</p> <p>337:13 reason.</p> <p>337:14 Q Was it an important part of the reason?</p> <p>337:16 A I don't know what other -- there were</p> <p>337:17 probably other reasons. I don't know them.</p>
<b>D. Cook Tr. at 337:23-338:11</b>	<p>337:23 Q The first is "Reliance on external ratings,"</p> <p>337:24 and within that bullet it reads, "Although we invest</p> <p>337:25 almost exclusively in AAA-rated securities, there is a</p> <p>338:2 concern that the rating agencies may not be properly</p> <p>338:3 assessing the risk in these securities."</p> <p>338:4 Do you see that?</p> <p>338:5 A Yes.</p> <p>338:6 Q Was there concern at Fannie Mae in 2005 that</p> <p>338:7 even with AAA-rated securities, the rating agencies</p> <p>338:8 may not be properly assessing the risk in PLS?</p> <p>338:10 A As stated here, it sounds like there was a</p> <p>338:11 concern.</p>
<b>Dallavecchia Tr. at 76:3-21</b>	<p>76:3 Q. And when you refer to</p> <p>76:4 instruments, Private Label Security is</p> <p>76:5 one example of a financial instrument; is</p> <p>76:6 that correct?</p> <p>76:7 A. Yes.</p> <p>76:8 Q. Okay. And so as the chief</p> <p>76:9 risk officer at Fannie Mae, did you make</p> <p>76:10 an effort to make sure that the senior</p> <p>76:11 leadership of Fannie Mae had an</p> <p>76:12 understanding -- excuse me, had a, quote,</p> <p>76:13 proper understanding of the risks</p> <p>76:14 associated with Private Label Securities?</p> <p>76:16 A. I think that in, in, in</p> <p>76:17 general -- in general, yes, I wanted to</p> <p>76:18 have, to ensure that we had an</p> <p>76:19 understanding of the risks associated</p> <p>76:20 with -- yes, an understanding of the risk</p> <p>76:21 of Private Label Securities.</p>
<b>Dallavecchia Tr. at 177:4-178:2</b>	<p>177:4 Q. Do you have any reason to</p> <p>177:5 believe that that kind of risk layering</p> <p>177:6 did not also exist in Private Label</p>

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	<p>177:7 Securities?</p> <p>177:9 A. I think I can only rephrase  177:10 what I just said. That the Private Label  177:11 Securities have a number of risks, of  177:12 which the combination of LTV, to the  177:13 borrower FICO, to the region where the  177:14 borrower is, to the structure of the  177:15 loan, to which tranche you are buying, to  177:16 which rep and warrants are provided with  177:17 the bond, who's guaranteeing the rep and  177:18 warrants, the counterparty risk, all of  177:19 those are risk factors.  177:20 So that, that would be my  177:21 statement, they are all risk factors that  177:22 need to be properly evaluated. And I'm  177:23 not an expert in it, but I, I recognize  177:24 they are, the ones that I mentioned are  177:25 among the multiples of the ones that need</p> <p>178:2 to be reviewed.</p>
<b>D. Cook Tr. at 68:19 – 69:5</b>	<p>68:19 Q What does it mean to size and price credit  68:20 risk in this context?</p> <p>68:21 A So sizing the deal was understanding the  68:22 risk associated with the deal and whether the  68:23 structure supported the senior tranches with -- that  68:24 we purchased. And then pricing was, you know, if --  68:25 if the credit of the deal was a AAA tranche, then they</p> <p>69:2 could infer a price that they would -- they would want  69:3 to receive, in other words, a yield that they would  69:4 want to receive. So if we paid par for a bond, we  69:5 would want to get a return above some benchmark.</p>
<b>Cao Tr. at 283:14-284:5</b>	<p>283:14 Q. What is risk layering?</p> <p>283:15 A. That's where we talk about the  283:16 correlations for this risk factors. It is  283:17 correlation of what risk factor is like.  283:18 Basically following sentence give you example,  283:19 right?</p> <p>283:20 So high LTV, low FICO. Those are  283:21 the, you know, two risks, two risks, yeah, risk  283:22 factors, right, and then if the loan observed  283:23 both of them by loan, that is risk vary, so one</p>

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	<p>283:24 loan has high LTV and low FICO. That's risk 283:25 layering.</p> <p>284:2 Q. So risk layering is more than one 284:3 risk factor together? 284:4 A. Together, yes, for one particular 284:5 loan..</p>
<b>Zhao Tr. at 658:2-660:12</b>	<p>Q. (BY MR. SACCA) Let me show you what we're marking as Exhibit 3567, FHFA05693580 through 81. The bottom e-mail on the first page is from Fan Xu -- how do you pronounce it?</p> <p>A. Fan Xu, yes.</p> <p>Q. Xu. -- to a group of people. Do you know who those people are in the "To" line?</p> <p>A. I know some of them. Like Gordon is her boss. Luis is -- may be her direct boss, like as a lower-level boss, or may be her colleague. They're all -- yeah, some of them are colleagues. They're all -- most of -- the names I know are researchers in Credit Research Department. Except Vanessa, actually. Vanessa is in David Gussmann's organization.</p> <p>Q. Okay. So these are colleagues of hers at Fannie Mae?</p> <p>A. It looks like it, yeah.</p> <p>Q. And she's sending them an article from that day's Wall Street Journal, October 30, 2008, titled "Ex-Fannie Mae Chief Mudd: Should Have Said 'No' More Often"?</p> <p>A. Yeah.</p> <p>Q. And you see the first line of the article is "Daniel Mudd says he should have said 'no' more often when he was chief executive officer of Fannie Mae"?</p> <p>A. Yeah, I saw that.</p> <p>Q. And then if you look on the second page of the e-mail, the first reported question there from the Wall Street Journal was "What were your main mistakes?"</p> <p>And Mr. Mudd's answer was, "I wish I'd said 'no' to more of the things the company was asked to do. We were asked -- or required -- to expand lending, to conserve capital while providing</p>

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	<p>liquidity, to meet housing goals for the underserved, to serve shareholders and homeowners alike. In a crisis of these proportions, something had to give. I should have gone to the government and gotten a clear answer to the question: What do you want -- more capital or more lending?</p> <p>"In 20/20 hindsight, I can go through and pick out loans I'd rather not have on the books."</p> <p>Ms. Xu sent you this e-mail also on October -- or this article also on October 30th, and she said "Have you seen this? Exactly as what you said - the executives should have said 'No' which what they are paid for."</p> <p>Had you been taking the position that Fannie Mae should have said no to having certain loans on its books?</p> <p>A. I don't remember the conversation I had with -- with Fan I guess. Have I been taking the -- I mean, I don't remember the specific conversation she was referring to.</p> <p>In terms of if you ask me have I taken the position to say no, I -- I would say probably yes after the crisis, like in '09 time frame, or '08, '09 time frame.</p>
<b>Kenneweg</b> <b>30(b)(6) Tr. at</b> <b>67:7 – 68:11</b>	<p>67:7 Q. What is your understanding of  67:8 the sentence "First NLC's guidelines make  67:9 exceptions largely unnecessary"?</p> <p>67:12 A. That they might have had  67:13 broader -- or broad enough guidelines to where  67:14 a lot of loans would comply with our  67:15 guidelines.</p> <p>67:16 Q. Loans that other subprime  67:17 lenders would not make. Right?</p> <p>67:20 A. That's what they've stated  67:21 here.</p> <p>67:22 Q. And do you see that they came  67:23 to that conclusion as a result of a loan-level  67:24 file review?</p> <p>68:3 A. Yes.</p> <p>68:4 Q. And do you see the</p>



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	<p>68:5 second-to-last sentence in that section says, 68:6 quote: "First NLC commented that they make 68:7 common sense underwriting decisions; we did 68:8 not see evidence of that in the file review"?</p> <p>68:11 A. I see that.</p>

Loosening of Underwriting Guidelines	
Cao Dep Tr. at 688:5-23	688:5 Q. But it was originators themselves 688:6 that were responsible for originating the loans 688:7 in compliance with those standards, right?
	688:9 THE WITNESS: Exactly. It was 688:10 someone else originate it, yes.
	688:11 BY MR. HARSCH:
	688:12 Q. So Fannie Mae didn't underwrite the 688:13 loans, correct? Fannie Mae set the standard by 688:14 which they were to be underwritten?
	688:16 THE WITNESS: We do have our 688:17 underwriting. We don't originate. Fannie Mae 688:18 never originate loans ourselves, so we do have 688:19 underwriting single-family, EU. It is a whole, 688:20 you know, team of people. They underwrite the 688:21 loans that we buy, so it doesn't matter, you 688:22 know, original or unoriginal or not, right, we 688:23 have our underwritten process, so that's...
	313:8 Q. One thing that changed between 313:9 2006 and summer of 2007, let's say, is the 313:10 performance of the economy, right?
	313:11 A. Performance of the economy, 313:12 housing prices started to go down, yes.
	313:13 Q. Is it correct to say it was 313:14 unknown in the 2006 time frame and early 313:15 2007 time frame how Alt-A mortgages would 313:16 perform in a significant downturn?
	313:18 A. There had been some modeling, 313:19 but probably the bigger issue was no one 313:20 knew how significant the downturn was 313:21 going to be.
	313:22 Q. And in fact a downturn of the 313:23 magnitude of what actually occurred was 313:24 not modeled, right?
Lockhart Tr. at 313:8-317:19	313:25 A. It was not modeled by Fannie  314:2 and Freddie; I think the worst one was 314:3 they looked at California and the Texas 314:4 oil patch as the two worst models, as I 314:5 remember.

**Loosening of Underwriting Guidelines**

314:6 Q. To your knowledge, did anyone  
 314:7 predict how bad the downturn would  
 314:8 actually be?

314:9 A. I mean, there is people in  
 314:10 retrospect that have said they did, but no  
 314:11 one told me at the time.

314:12 Q. I take it no one told you at  
 314:13 the time how Alt-A mortgages would perform  
 314:14 in the face of the very substantial  
 314:15 downturn that we in fact had in the  
 314:16 economy?

314:18 A. They were modeling, as I said,  
 314:19 the Texas oil patch and the California ups  
 314:20 and downs, and so they did modeling and  
 314:21 significant modeling with those kinds of  
 314:22 scenarios and certainly this showed there  
 314:23 would be losses, but not losses of the  
 314:24 magnitude as it turned out.

314:25 Q. What caused the losses of the

315:2 magnitude as it turned out, as you  
 315:3 referred to?

315:5 A. Well, as you just said, the  
 315:6 economy, people losing their jobs.

315:7 As I've said many times, poor  
 315:8 underwriting and selling products to  
 315:9 people that shouldn't have gotten those  
 315:10 products.

315:11 Q. My last set of questions was  
 315:12 about the Alt-A mortgages.

315:13 Would it also be accurate to  
 315:14 say that the performance of subprime  
 315:15 mortgages in a significant economic  
 315:16 downturn was not known in the 2006, early  
 315:17 2007 time frame?

315:19 A. I think you could say that  
 315:20 people knew that performance was going to  
 315:21 be poor if there was going to have a  
 315:22 significant downturn, but subprime  
 315:23 mortgages have been around for a while.

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315:24 What happened again is the  
315:25 characteristics of subprime mortgages have

316:2 changed over the period of the 2000s and  
316:3 they became more risky.

316:4 Again, the teaser mortgages and  
316:5 some of the other things that were written  
316:6 at that point, there wasn't enough  
316:7 knowledge to know what would happen to  
316:8 those mortgages.

316:9 Although you have to assume,  
316:10 you know, if we had what we had, there  
316:11 were going to be losses.

316:12 Q. Did you at OFHEO in the 2006  
316:13 through first half of 2007 time frame know  
316:14 that the characteristics of subprime  
316:15 mortgages had changed in the way you just  
316:16 mentioned?

316:18 A. We knew, I think we saw some  
316:19 charts earlier that I used in some of my  
316:20 presentations that there was less  
316:21 documentation going on, we knew there was  
316:22 more 228s and 327s and all those kinds of  
316:23 securities being written, yes.

316:24 Q. 228s and 337s refer to types of  
316:25 subprime mortgages, right?

317:2 A. Yes, they are basically --  
317:3 two-year had a real teaser mortgage rate  
317:4 and then the next 28 had a much higher  
317:5 rate and the problem was that oftentimes  
317:6 people were only expecting to have the  
317:7 mortgage for two years because they  
317:8 thought housing prices were going to go up  
317:9 and could refinance; all of a sudden when  
317:10 housing prices didn't go up they couldn't  
317:11 refinance and they ended up with these  
317:12 much higher rates they couldn't afford.

317:13 Q. Just to be clear on the record,  
317:14 a 337 refers to a three-year teaser  
317:15 rate --

317:16 A. 27.

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	<p>317:17 Q. 27.</p> <p>317:18 Year period of a higher rate?</p> <p>317:19 A. Right</p>
<b>Kenneweg Tr. at 315:20 – 316:12</b>	<p>315:20 Q. The next paragraph reads: "Credit</p> <p>315:21 trends. The need for a 'affordability</p> <p>315:22 products' (in response to rising home prices in</p> <p>315:23 relation to income) in addition to the</p> <p>315:24 favorable credit environment led to the</p> <p>315:25 pervasive loosening of credit standards in</p> <p>316:2 originator's underwriting guidelines. Now, the</p> <p>316:3 combination of lower HPA and aggressive</p> <p>316:4 underwriting practices have begun to show up in</p> <p>316:5 delinquency and EPD figures."</p> <p>316:6 Do you see that?</p> <p>316:7 A. I do.</p> <p>316:8 Q. And do you recall that being the</p> <p>316:9 state of things at the end of 2006?</p> <p>316:11 THE WITNESS: I recall these general</p> <p>316:12 themes; yes.</p>
<b>Bates Moss Tr. at 163:7 – 163:19</b>	<p>163:7 Q. Are you aware of your group</p> <p>163:8 ever disapproving or placing on caution</p> <p>163:9 an originator because a substantial</p> <p>163:10 portion of the loans they generated did</p> <p>163:11 not meet their underwriting guidelines?</p> <p>163:14 A. I am not aware of a specific</p> <p>163:15 instance. Again, it should be documented</p> <p>163:16 if that were the case.</p> <p>163:17 Q. And have you seen any such</p> <p>163:18 documents?</p> <p>163:19 A. No, I have not.</p>
<b>Bates Moss Tr. at 448:10 – 452:6</b>	<p>448:10 Q. What did you mean that these</p> <p>448:11 attempts by Ameriquest and New Century to</p> <p>448:12 get market share will likely result in</p> <p>448:13 deterioration of performance metrics?</p> <p>448:14 A. That based upon what</p> <p>448:15 information we were receiving from</p> <p>448:16 analyst reports and other documents, that</p> <p>448:17 this was certainly something that was</p> <p>448:18 raised in those reports. So we were</p> <p>448:19 using this as an opportunity to</p>

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448:20 disseminate information on the whole loan  
 448:21 side regarding our subprime activity.  
 448:22 Q. Did you have an understanding  
 448:23 about the substance of what you were  
 448:24 saying here, that the substance of how  
 448:25 attempts to get market share was linked

449:2 to deteriorating performance?

449:3 A. Yes.

449:4 Q. And how is it that trying to  
 449:5 get market share is linked to a  
 449:6 deterioration in performance metrics?

449:7 A. One such example is that in an  
 449:8 effort to grow market share, companies  
 449:9 may become more aggressive in their  
 449:10 underwriting.

449:11 Q. What do you mean by aggressive  
 449:12 in underwriting?

449:13 A. That they may change their,  
 449:14 maybe loosen their standards potentially.  
 449:15 They could, you know, take other steps.  
 449:16 This was just an attempt to ensure that  
 449:17 in reviewing these whole loans, that  
 449:18 particularly given the fact that New  
 449:19 Century and Ameriquest at that time were  
 449:20 already on our watch list, that we paid  
 449:21 closer attention in monitoring.

449:22 Q. What do you mean when you say  
 449:23 that underwriters or originators may  
 449:24 loosen their standards potentially?

449:25 A. Every company that originates,

450:2 underwrites, sells, services assets  
 450:3 typically has a process in place and a  
 450:4 credit box where they have criteria for  
 450:5 how they will underwrite a transaction.

450:6 Q. And you -- finish?

450:7 A. Companies make, managements  
 450:8 make decisions about that credit box.

450:9 Q. And you understood that to get  
 450:10 market share companies may decide to  
 450:11 loosen their underwriting criteria?

450:12 A. Not all companies.

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450:13 Q. Some?  
 450:14 A. Some.  
 450:15 Q. Like New Century and  
 450:16 Ameriquest?  
 450:17 A. Based upon information that  
 450:18 was coming in from the marketplace, yes.  
 450:19 Q. And did you understand that  
 450:20 when these companies loosened their  
 450:21 credit box there's a risk that they will  
 450:22 issue lower quality loans?

450:25 A. There is a risk that companies

451:2 will be willing to take on or to enter  
 451:3 into transactions that have higher risk  
 451:4 profiles, yes.  
 451:5 Q. And here you indicate that  
 451:6 with respect to New Century and  
 451:7 Ameriquest, who are trying to get market  
 451:8 share, that it will likely result in  
 451:9 deterioration in performance metrics,  
 451:10 correct?  
 451:11 A. That's correct.  
 451:12 Q. Why did you think it would  
 451:13 likely result in deterioration of their  
 451:14 performance metrics?  
 451:15 A. Because based upon our ongoing  
 451:16 monitoring of these particular credits,  
 451:17 we had already started to see  
 451:18 deterioration in their metrics.  
 451:19 Q. And by metrics, what do you --  
 451:20 what are you referring to?  
 451:21 A. I.e., FICO's, other financial  
 451:22 metrics related to leverage, debt to  
 451:23 service cover, all of those.  
 451:24 Q. And would it also include the  
 451:25 metrics by which the risk of loans are

452:2 measured?

452:4 Q. Such as FICO?  
 452:5 A. Yes, we could look at that  
 452:6 information, yes.

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<b>Bates Moss Tr. at 454:20 – 455:7</b>	<p>454:20 Q. Can you identify any</p> <p>454:21 originator that informed you or your</p> <p>454:22 group that they always, universally,</p> <p>454:23 absolutely issue loans consistent with</p> <p>454:24 their underwriting guidelines?</p> <p>455:2 form.</p> <p>455:3 Q. No exception?</p> <p>455:6 A. I don't recall having those</p> <p>455:7 conversations, no.</p>
<b>Bates Moss Tr. at 456:3 – 456:16</b>	<p>456:3 Q. And what you write is "My</p> <p>456:4 understanding is that credit standards</p> <p>456:5 are loosening." Do you see that?</p> <p>456:6 A. Yes.</p> <p>456:7 Q. And what did you mean when you</p> <p>456:8 wrote to Mr. Grimes and these other</p> <p>456:9 people including Mr. Norris that credit</p> <p>456:10 standards are loosening?</p> <p>456:11 A. What I stated earlier is that</p> <p>456:12 when -- sometimes companies make a</p> <p>456:13 decision, management teams make a</p> <p>456:14 decision to open up their credit box and</p> <p>456:15 that means having a wider range of</p> <p>456:16 criteria that they are comfortable with.</p>
<b>Bates Moss Tr. at 456:18 – 456:22</b>	<p>456:18 Did you understand that</p> <p>456:19 originators were issuing loans that</p> <p>456:20 perhaps previously they would not have</p> <p>456:21 issued when -- before they loosened their</p> <p>456:22 standards?</p>
<b>Bates Moss Tr. at 456:24 – 457:4</b>	<p>456:24 A. Based on this statement, what</p> <p>456:25 I was saying was that there was a shift.</p> <p>457:2 I wasn't making a statement about any</p> <p>457:3 specific originator, but this was a</p> <p>457:4 trend.</p>
<b>Bates Moss Tr. at 461:5 – 461:19</b>	<p>461:5 Q. Did you find anything during</p> <p>461:6 those onsite reviews or have anything</p> <p>461:7 reported to you from those onsite reviews</p> <p>461:8 that was inconsistent with your</p> <p>461:9 understanding that credit standards were</p> <p>461:10 loosening in March of 2006?</p> <p>461:13 A. I don't recall that being a</p>



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	<p>461:14 specific issue. As I stated before,  461:15 there was a ton of market research  461:16 available during this time because the  461:17 overall market was starting to report  461:18 more frequently on these topics. So this  461:19 is pretty standard.</p>
<b>Bates Moss Tr. at 467:15 – 468:3</b>	<p>467:15 Q. And you were also in the email  467:16 above that able to communicate with Mr.  467:17 Norris and others within Fannie Mae your  467:18 understanding that credit standards are  467:19 loosening, correct?</p> <p>467:22 A. I made a general statement  467:23 around credit standards loosening, yes.  467:24 Q. And that statement wasn't  467:25 limited to any particular originator, it</p> <p>468:2 was a general statement about the --  468:3 A. The industry, yes.</p>
<b>Bates Moss Tr. at 597:2 – 597:16</b>	<p>597:2 Q. And would looser underwriting  597:3 criteria also be contributing factors to  597:4 increased early payment defaults?</p> <p>597:6 A. Less restrictive criteria  597:7 along with a number of other factors  597:8 could contribute to early payment  597:9 default. I'm not sure exactly what your  597:10 point is.  597:11 Q. Did you understand that at the  597:12 time when you were working at Fannie Mae?</p> <p>597:15 A. I understood that before I  597:16 joined Fannie Mae, so.</p>
<b>Bates Moss Tr. at 649:12 – 650:6</b>	<p>649:12 Q. Well your review team would go  649:13 around and go to originators and review  649:14 their practices, right?  649:15 A. We would review those  649:16 practices, policies and procedures, and  649:17 as evidenced in the documents that you've  649:18 put in front of me, those processes were  649:19 described, yes.  649:20 Q. And do you recall that among  649:21 the processes that were reported to you</p>

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	<p>649:22 by your review team were that originators  649:23 from time to time were making loans that  649:24 did not strictly meet their underwriting  649:25 guidelines?</p> <p>650:4 A. What we observed in that  650:5 process is that they had built into their  650:6 process escalation and exceptions, yes.</p>
<b>Feigles Tr. at 210:21 – 212:5</b>	<p>210:21 Q. And then your final paragraph is:  210:22 "We will always look at and form our own  210:23 opinion about lender's guidelines and for very  210:24 liberal guidelines, we would expect to see  210:25 stricter processes or controls and we would</p> <p>211:2 have a lower tolerance for deviations from  211:3 those processes."  211:4 Do you see that?  211:5 A. I see that.  211:6 Q. What did you mean by that?  211:7 A. It appears to be fairly  211:8 straightforward that we are going to form our  211:9 own opinions about the lender's guidelines.  211:10 I'm not sure I can summarize that more.  211:11 Q. Okay. So when you refer to lower  211:12 tolerances for deviations from those processes,  211:13 are you referring to deviations from the  211:14 underwriting guidelines?  211:15 A. Yeah, my -- what I would believe I  211:16 am saying there is we'd look for fewer  211:17 exceptions.  211:18 Q. So is it fair to summarize this as  211:19 -- in a case where you would assess a  211:20 counterparty to have liberal guidelines, you  211:21 would expect more compliance with the  211:22 guidelines, and where there were stricter  211:23 guidelines in place, you might accept a -- have  211:24 a greater tolerance for deviation from the  211:25 underwriting guidelines?</p> <p>212:3 THE WITNESS: Well, again, I think  212:4 what we expect to see is fewer exceptions  212:5 utilized with more liberal guidelines.</p>

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Aneiro Tr. at 257:1 - 258:25	257:1 Q. Can you tell me what this is,
	257:2 please?
	257:3 A. This is the nonagency mortgage
	257:4 ABS credit analysis procedure guide.
	257:5 Q. What is it used for? What was
	257:6 it used for?
	257:7 A. It is the procedure for the
	257:8 credit group to analyze the credit of a
	257:9 nonagency mortgage security.
	257:10 Q. And let's turn to page FHFA
	257:11 11625650, which is the second page of the
	257:12 document. Do you see at the top of the
	257:13 page where it says "the MABS credit
	257:14 analysis process can be divided into
	257:15 three steps"?
	257:16 A. Yes.
	257:17 Q. And do you see where it says
	257:18 the three steps are costing, counterparty
	257:19 risk assessment and surveillance?
	257:20 A. Yes.
	257:21 Q. Are those the three steps into
	257:22 which the MABS credit analysis process
	257:23 could be divided?
	257:24 A. It certainly says that here.
	257:25 Q. Do you agree?
	258:1 A. I have no reason to disagree.
	258:3 A. It's not my guideline. It was
	258:4 not my guideline.
	258:6 Q. Are you aware of any other
	258:7 steps that go into the MABS credit
	258:8 analysis process?
	258:9 A. Not that I recall.
	258:10 Q. Looking at the counterparty
	258:11 risk assessment bullet point there, do
	258:12 you see where it says "counterparty risk
	258:13 assessment recognizes that financially
	258:14 and/or operationally distressed servicers
	258:15 and originators can adversely impact
	258:16 collateral performance and also expose
	258:17 Freddie Mac to reputational risk"?

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	<p>258:18 Do you see that?</p> <p>258:19 A. I do see that.</p> <p>258:20 Q. Do you agree that financially</p> <p>258:21 and/or operationally distressed servicers</p> <p>258:22 and originators can adversely impact</p> <p>258:23 collateral performance and also expose</p> <p>258:24 Freddie Mac to reputational risk?</p> <p>258:25 A. I do.</p>
<b>Kenneweg 30(b)(6) Tr. at 75:18 – 76:5</b>	<p>75:18 Q. Would if have been your regular</p> <p>75:19 practice, when receiving a review like this,</p> <p>75:20 to advise Freddie Mac to stop buying PLS</p> <p>75:21 backed by First NLC loans?</p> <p>75:22 A. Not necessarily.</p> <p>75:23 Q. Why not?</p> <p>75:24 A. There were policies and</p> <p>75:25 procedures that set guidelines for how to</p> <p>76:2 consume this information and how it should be</p> <p>76:3 used, and within those guidelines it did not</p> <p>76:4 say stop purchases for marginal reviews,</p> <p>76:5 so ...</p>
<b>Wood Tr. at 323:16-326:2</b>	<p>323:16 Q. You can take 32214 off. This has</p> <p>323:17 already been marked as Exhibit 1826. It's a</p> <p>323:18 June 16th, 2006 e-mail and attachment from Mary</p> <p>323:19 Jo Whipple to a number of people, including</p> <p>323:20 you. Subject is: "E-Store AMO Origination</p> <p>323:21 Review, First NLC Financial Services." Bates</p> <p>323:22 number is FHFA 0348420.</p> <p>323:23 Do you see that?</p> <p>323:24 A. 203?</p> <p>323:25 Q. Yes, you're right. I'm sorry.</p> <p>324:2 A. Uh-uh.</p> <p>324:3 Q. 203.</p> <p>324:4 A. Yes, I see it.</p> <p>324:5 Q. Who is Mary Jo Whipple?</p> <p>324:6 A. Mary Jo Whipple provided, I believe,</p> <p>324:7 administrative support in the AMO group.</p> <p>324:8 Q. Did she have any substantive role or</p> <p>324:9 was it mostly administrative?</p> <p>324:10 A. Mostly administrative.</p> <p>324:11 Q. And do you see your name on the</p> <p>324:12 first line of the "to" field?</p>

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	324:13	A. Yes. Uh-huh.
	324:14	Q. And do you recall receiving this
	324:15	document?
	324:16	A. No. This, again, looks like a
	324:17	standard distribution of an AMO report that I
	324:18	would get from time to time. So nothing -- no
	324:19	earlier or memorable -- memorable about this
	324:20	particular report.
	324:21	Q. And you stated that sometimes you
	324:22	read these reports and sometimes you didn't?
	324:23	A. That's right.
	324:24	Q. And there was no rule you had as to
	324:25	when to read them and when not to read them?
	325:2	A. No, not really. Again, they didn't
	325:3	impact my -- they didn't impact my job
	325:4	responsibility as much for me.
	325:5	Q. Can you turn to the attachment?
	325:6	It's the document ending 206. And this has the
	325:7	familiar review area and rating matrix at the
	325:8	top.
	325:9	Do you see that?
	325:10	A. Uh-huh.
	325:11	Q. And here, the reviews are credit,
	325:12	marginal, do you see that?
	325:13	A. Yeah.
	325:14	Q. Appraisal, marginal?
	325:15	Do you see that?
	325:16	A. Uh-huh.
	325:17	Q. Management, satisfactory, do you see
	325:18	that?
	325:19	A. Yes.
	325:20	Q. And controls, marginal, do you see
	325:21	that?
	325:22	A. Uh-huh.
	325:23	Q. And these are improvements over the
	325:24	poor, poor satisfactory and poor rating from
	325:25	the prior review, correct?
	326:2	A. It appears so, yeah.
<b>Palmer Tr. at 491:16 – 492:13; 492:22 -- 493:20</b>	491:16	Q. Assessing those was left to
	491:17	the judgment of the credit approval team,
	491:18	the MABS team that you were part of,

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491:19 right?

491:21 A. It was similar credit review.  
491:22 Any AMO score below a certain level  
491:23 required additional work. Generally  
491:24 speaking, marginals may cause us pause or  
491:25 may cause us to read the AMO review to

492:2 understand why it was rated marginal. I  
492:3 don't remember specifically on this one  
492:4 what it was or anything more specifics  
492:5 about that.

492:6 Q. Other than reading the AMO  
492:7 review, was there any other additional  
492:8 work that you would do in response to a  
492:9 marginal or poor grade?

492:10 A. We could call up Ron Feigles  
492:11 or somebody in his group to better  
492:12 understand the reason behind it being  
492:13 marginal.

....

492:22 Q. Other than reading the AMO  
492:23 review and perhaps speaking with Mr.  
492:24 Feigles and his group, was there any  
492:25 other additional work that you would do

493:2 in response to seeing a marginal or poor  
493:3 grade?

493:4 A. I believe some of these  
493:5 counterparties were also rated by the  
493:6 rating agencies and looking at what the  
493:7 rating agencies' review were -- was for  
493:8 those counterparties.

493:9 Q. And how would you get that  
493:10 information?

493:11 A. We had access through a  
493:12 subscription to the rating agencies'  
493:13 websites and looking them up there.

493:14 Q. Aside from reading the AMO  
493:15 review, talking to Ron Feigles, perhaps,  
493:16 and perhaps looking at rating agency

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	<p>493:17 ratings on originators, was there  493:18 anything else you would do in response to  493:19 seeing a poor or marginal grade?  493:20 A. Not that I remember.</p>
<b>Palmer Tr. at 747:21 -- 748:16; 748:22 -- 749:2</b>	<p>747:21 Q. Was it your practice to review  747:22 AMO reviews of the aggregators on deals  747:23 that you were approving credit for?  747:24 A. On aggregators, I believe many  747:25 of them I did review. I would especially</p> <p>748:2 review those that were marginal or poor,  748:3 if there were any.  748:4 Q. What was your understanding of  748:5 the purpose of these review?  748:6 A. To assess the risk management  748:7 and control practices of the aggregator.  748:8 Q. And to ensure that they had  748:9 good risk management and control  748:10 practices?  748:11 A. To understand what those, what  748:12 those practices were.  748:13 Q. And then to provide a rating  748:14 to those practices?  748:15 A. Yes, they would assess the  748:16 rating relative to those practices.  . . . .</p> <p>748:22 Q. Were you aware that Freddie  748:23 Mac would send people to do onsite visit  748:24 at the aggregators and review their  748:25 policies and procedures?</p> <p>749:2 A. Yes.</p>
<b>Kenneweg 30(b)(6) Tr. at 142:17-144:12</b>	<p>142:17 And then the second spreadsheet  142:18 in Exhibit 1828, Ms. Kenneweg, tracks Freddie  142:19 Mac's exposure in PLS by issuer, is that  142:20 correct?</p> <p>142:24 A. That's correct.  142:25 Q. And is the information that</p> <p>143:2 kind of is to the left of the grid also just  143:3 ID numbers?</p>

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	<p>143:4 A. I believe so.</p> <p>143:5 Q. Is this a document that you,</p> <p>143:6 yourself, tracked and maintained?</p> <p>143:7 A. Yes.</p> <p>143:8 Q. If you then turn to the first</p> <p>143:9 page of Exhibit 1828, you'll see a chart</p> <p>143:10 labeled "Non-Agency Mortgage ABS Portfolio</p> <p>143:11 Concentrations," do you see that?</p> <p>143:12 A. I do.</p> <p>143:13 Q. And is this a chart that you</p> <p>143:14 generated from the spreadsheets we just</p> <p>143:15 referred to?</p> <p>143:16 A. I believe so.</p> <p>143:17 Q. And it shows Freddie Mac's top</p> <p>143:18 ten originators, servicers, issuers and</p> <p>143:19 trustees in the PLS space, is that right?</p> <p>143:20 A. It is.</p> <p>143:21 Q. And their corresponding metrix</p> <p>143:22 scores, correct?</p> <p>143:23 A. Yes.</p> <p>143:24 Q. And did you circulate this</p> <p>143:25 document on a monthly basis?</p> <p>144:2 A. I did.</p> <p>144:3 Q. And is it correct that this</p> <p>144:4 document reflects that as of June 2007 Freddie</p> <p>144:5 Mac's top five originators, in terms of their</p> <p>144:6 exposure through PLS, all had ratings of</p> <p>144:7 marginal from their operational reviews?</p> <p>144:8 A. According to this document,</p> <p>144:9 that's correct.</p> <p>144:10 Q. And would you expect this</p> <p>144:11 document would be correct?</p> <p>144:12 A. I would.</p>
<b>Kenneweg 30(b)(6) Tr. at 42:23 – 43:22</b>	<p>42:23 Q. We haven't been that</p> <p>42:24 productive. And could you identify the</p> <p>42:25 document that I have just handed you?</p> <p>43:2 A. It looks like an e-mail. The</p> <p>43:3 subject is MABS Policies/Procedures.</p> <p>43:4 Q. Is this an e-mail from you?</p> <p>43:5 A. It is.</p> <p>43:6 Q. That you sent on or about</p>



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	<p>43:7 December 10, 2009?</p> <p>43:8 A. Yes.</p> <p>43:9 Q. And what are you attaching to</p> <p>43:10 this e-mail?</p> <p>43:11 A. It looks like a procedure for</p> <p>43:12 PLS counterparty. Let's see what else. And a</p> <p>43:13 policy and procedure, um, also related to PLS,</p> <p>43:14 owned by another area.</p> <p>43:15 Q. Okay. So the document we have</p> <p>43:16 attached is MABS Counterparty Procedure Number</p> <p>43:17 123. Right?</p> <p>43:18 A. Yes.</p> <p>43:19 Q. And is that what is attached to</p> <p>43:20 this e-mail, the MABS Counterparty Procedure</p> <p>43:21 123?</p> <p>43:22 A. It is.</p>
<b>Kenneweg 30(b)(6) Tr. at 44:8 – 13</b>	<p>44:8 Q. Do you recall this being in</p> <p>44:9 effect during the period 2005 through 2007?</p> <p>44:10 A. Yes, it would have been</p> <p>44:11 sometime after I was hired.</p> <p>44:12 Q. But before December 2007?</p> <p>44:13 A. Yes. Yes.</p>
<b>Kenneweg 30(b)(6) Tr. at 44:24 - 25</b>	<p>44:24 Q. Who drafted this procedure?</p> <p>44:25 A. I did.</p>
<b>Kenneweg Tr. 30(b)(6) at 45:5 – 8</b>	<p>45:5 Q. And what was the purpose for</p> <p>45:6 this being adopted?</p> <p>45:7 A. In order to have a framework</p> <p>45:8 for me to operate.</p>
<b>Kenneweg Tr. 30(b)(6) at 45:17 – 47:22</b>	<p>45:17 Q. Well, what do you mean by, "for</p> <p>45:18 me to operate"?</p> <p>45:19 A. This is an overview of the</p> <p>45:20 processes that I would follow in order to</p> <p>45:21 approve and monitor the PLS counterparties.</p> <p>45:22 Q. Is it still in effect?</p> <p>45:23 A. No. Not this exact policy.</p> <p>45:24 No.</p> <p>45:25 Q. Was it replaced?</p> <p>46:2 A. Or procedure, I mean. Um, not</p> <p>46:3 directly.</p> <p>46:4 Q. Was it just nullified?</p>

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	<p>46:7 A. I'm -- I'm not sure what became  46:8 of -- of this exact procedure.  46:9 Q. Do you recall why it was deemed  46:10 not to control any longer?  46:11 A. There was a  46:12 no-purchase-directive in the portfolio.  46:13 Q. And when did that occur?  46:14 A. I don't recall the exact date.  46:15 Q. Was that before or after the  46:16 conservatorship?  46:17 A. I don't recall.  46:18 Q. And simultaneous, or near the  46:19 time of the no-purchase-directive, I guess  46:20 there was no need to follow MABS 123 anymore?  46:21 A. Yeah, not a need to do  46:22 everything that's outlined in the procedure.  46:23 That's right.  46:24 Q. Now, if you look at the, kind  46:25 of near the bottom of the first page of the</p> <p>47:2 procedure, there's a section that's called  47:3 Data Sources For Financial Analysis.  47:4 Do you see that?  47:5 A. Yes.  47:6 Q. And the last of the sources  47:7 mentioned are Alternative Markets, Operations,  47:8 Written Reviews. Do you see that?  47:9 A. Yes.  47:10 Q. Now, is that a series of  47:11 reviews put out by the AMO department that you  47:12 spoke of earlier?  47:13 A. It is, yes.  47:14 Q. Mr. Feagle's group?  47:15 A. Mm-hmm.  47:16 Q. And where did Mr. --  47:17 MR. SECHLER: Strike that.  47:18 BY MR. SECHLER:  47:19 Q. Where did AMO fall within the  47:20 Freddie organizational structure?</p> <p>47:22 A. I don't know.</p>
<b>Kenneweg 30(b)(6) Tr. at</b>	<p>48:16 Q. How large was the department?  48:17 A. Alternative markets operations?</p>

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<b>48:16 – 24</b>	<p>48:18 Q. Yes.</p> <p>48:19 A. Probably about six or seven</p> <p>48:20 people.</p> <p>48:21 Q. And were those people all</p> <p>48:22 people who performed operational reviews?</p> <p>48:23 A. They had an admin at one point.</p> <p>48:24 But yeah, for the most part. Yes.</p>
<b>Kenneweg 30(b)(6) Tr. at 49:5 - 24</b>	<p>49:5 Q. What policies and procedures</p> <p>49:6 governed AMO?</p> <p>49:7 A. There was an overall policy, I</p> <p>49:8 believe there was one from 2005, and a later</p> <p>49:9 one from 2007, an overall policy that was</p> <p>49:10 comprised of a lot of procedures, which I</p> <p>49:11 believe is in the binder.</p> <p>49:12 Q. Okay. You can go ahead and --</p> <p>49:13 feel free to consult the binder. And if you</p> <p>49:14 could point out the policy you're referring</p> <p>49:15 to, that would be great.</p> <p>49:16 A. Sure. If you turn to Tab 4L.</p> <p>49:17 Q. Yes.</p> <p>49:18 A. So this is the overall policy</p> <p>49:19 which I said is composed of several</p> <p>49:20 procedures.</p> <p>49:21 Q. Now, the index indicates that</p> <p>49:22 Tab 4L is dated December 17, 2007?</p> <p>49:23 A. Is that a question? I'm sorry.</p> <p>49:24 Q. Yes. Do you see that?</p>
<b>Kenneweg 30(b)(6) Tr. at 50:4 – 19</b>	<p>50:4 A. Okay. I see it.</p> <p>50:5 Q. So was there a -- a procedure</p> <p>50:6 in place for AMO covering the same topics as</p> <p>50:7 Tab 4L prior to December 2007?</p> <p>50:8 A. I thought there was, but -- let</p> <p>50:9 me just flip through some of the other tabs in</p> <p>50:10 here and see if I'm thinking of something</p> <p>50:11 else.</p> <p>50:12 ---</p> <p>50:13 (Witness reviewing document.)</p> <p>50:14 ---</p> <p>50:15 A. I mean, there's lots of</p> <p>50:16 supporting documents that have been drafted,</p> <p>50:17 giving an overview to their framework.</p> <p>50:18 There's job checklists. Here's the --</p> <p>50:19 actually, here are the procedures.</p>

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<b>Kenneweg Tr. 30(b)(6) at 51:3 – 25</b>	<p>51:3 Q. And is Tab 4A the set of 51:4 procedures that governed AMO in August 2005? 51:5 A. That's my understanding. I 51:6 mean, just from reading the document. 51:7 Q. Well, your understanding is 51:8 you're here giving testimony on behalf of 51:9 Freddie Mac -- 51:10 A. Right. 51:11 Q. -- as to the policies and 51:12 procedures of, among other things, AMO? 51:13 A. Right, and --</p> <p>51:15 A. And from reading the document, 51:16 this seems consistent with my understanding of 51:17 their practices at that time period. 51:18 Q. Did you notice that Tab L, 51:19 which you referred to earlier, is a red-lined 51:20 version? 51:21 A. I did. 51:22 Q. Is that the final set of 51:23 policies that were effective December 2007 for 51:24 AMO? 51:25 A. To the best of my knowledge.</p>
<b>Kenneweg Tr. 30(b)(6) at 52:22 - 55:19</b>	<p>52:22 Q. Yes. Were AMO reviews 52:23 conducted on originators whose loans backed 52:24 PLS securities?</p> <p>53:2 form. 53:3 A. Yes. 53:4 Q. And in those reviews what 53:5 information was considered by AMO? 53:6 A. Credit guidelines. I mean, 53:7 there were a number of different categories, 53:8 but at a high level my recollection is credit 53:9 guidelines. Quality control. Compliance. 53:10 Overall controls at the company. So, you 53:11 know, sometimes it probably varied, depending 53:12 on the exact business model of the 53:13 counterparty. But at a high level those were 53:14 some of the topics. 53:15 Q. When you say "credit 53:16 guidelines," do you mean underwriting 53:17 guidelines?</p>

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53:18 A. Yes.  
53:19 Q. And did the AMO reviews involve  
53:20 loan-level review?

53:22 A. What type of AMO reviews?  
53:23 Q. Of originators.  
53:24 A. Yes.  
53:25 Q. And was the purpose of the

54:2 review, among other things, speaking again of  
54:3 originators, to determine the originators'  
54:4 compliance with their underwriting guidelines?

54:6 A. My understanding was the  
54:7 reviews were not to serve so much as an audit  
54:8 on their compliance; it was more to get an  
54:9 understanding of the riskiness of their  
54:10 guidelines, and to get a sense for the types  
54:11 of loans they were underwriting.

54:12 Q. And whether or not those loans  
54:13 were of poor credit quality?

54:15 A. Um, not just of poor credit  
54:16 quality, but to be able to provide an  
54:17 assessment of the average loan quality.

54:18 Q. And to determine whether or not  
54:19 the documentation in the loan file was  
54:20 consistent with what Freddie Mac expected?

54:22 BY MR. SECHLER:  
54:23 Q. Right?  
54:24 A. I am -- I'm not sure about that  
54:25 specifically.

55:2 Q. To identify concerns with the  
55:3 originators' underwriting processes?

55:5 A. That's, again, very specific.  
55:6 Q. What do you mean, that's very  
55:7 specific?  
55:8 A. I didn't actually attend the  
55:9 loan file reviews, so your questions are about  
55:10 the loan file reviews.

<b>GSE Counterparty Reviews and Policies</b>	
	<p>55:11 Q. But you read the AMO</p> <p>55:12 operational reviews, didn't you?</p> <p>55:13 A. I did. And I attended one of</p> <p>55:14 the onsite management meetings. One of the</p> <p>55:15 portions, yes.</p> <p>55:16 Q. How many AMO operational</p> <p>55:17 reviews did you review between 2005 and 2007?</p> <p>55:19 A. I didn't count.</p>
<b>Kenneweg 30(b)(6) Tr. at 56:5 -- 23</b>	<p>56:5 Q. Did AMO indicate in the report</p> <p>56:6 whether or not they conducted a loan-level</p> <p>56:7 review?</p> <p>56:8 A. I believe they did.</p> <p>56:9 Q. Do you recall that AMO also</p> <p>56:10 reviewed originators' appraisal practices?</p> <p>56:12 A. Are you talking about during</p> <p>56:13 the loan file review, or just overall in</p> <p>56:14 their --</p> <p>56:15 Q. In their operational review.</p> <p>56:16 A. Yes, that would have been part</p> <p>56:17 of what they would review, yes.</p> <p>56:18 Q. Now, you mentioned that you</p> <p>56:19 attended one meeting that was kind of related</p> <p>56:20 to AMO's reviews?</p> <p>....</p> <p>56:23 A. Oh, I'm sorry. Yes.</p>
<b>Kenneweg 30(b)(6) Tr. at 40:23-41:12</b>	<p>40:23 Q. Yes. Please identify, if you</p> <p>40:24 would, all departments or business units</p> <p>40:25 within Freddie Mac who were involved in the</p> <p>41:2 review or evaluation of PLS counterparties.</p> <p>41:4 A. What type of --</p> <p>41:7 A. What type of review and</p> <p>41:8 evaluation?</p> <p>41:9 Q. Any review that involves</p> <p>41:10 considering information concerning those</p> <p>41:11 counterparties, forming an opinion, rendering</p> <p>41:12 an evaluation, or issuing an approval.</p>
<b>Kenneweg 30(b)(6) Tr. at</b>	<p>42:23 Q. We haven't been that</p> <p>42:24 productive. And could you identify the</p>

<b>GSE Counterparty Reviews and Policies</b>	
<b>42:23-43:22</b>	<p>42:25 document that I have just handed you?</p> <p>43:2 A. It looks like an e-mail. The</p> <p>43:3 subject is MABS Policies/Procedures.</p> <p>43:4 Q. Is this an e-mail from you?</p> <p>43:5 A. It is.</p> <p>43:6 Q. That you sent on or about</p> <p>43:7 December 10, 2009?</p> <p>43:8 A. Yes.</p> <p>43:9 Q. And what are you attaching to</p> <p>43:10 this e-mail?</p> <p>43:11 A. It looks like a procedure for</p> <p>43:12 PLS counterparty. Let's see what else. And a</p> <p>43:13 policy and procedure, um, also related to PLS,</p> <p>43:14 owned by another area.</p> <p>43:15 Q. Okay. So the document we have</p> <p>43:16 attached is MABS Counterparty Procedure Number</p> <p>43:17 123. Right?</p> <p>43:18 A. Yes.</p> <p>43:19 Q. And is that what is attached to</p> <p>43:20 this e-mail, the MABS Counterparty Procedure</p> <p>43:21 123?</p> <p>43:22 A. It is.</p>
<b>Kenneweg 30(b)(6) Tr. at 49:5-49:24</b>	<p>49:5 Q. What policies and procedures</p> <p>49:6 governed AMO?</p> <p>49:7 A. There was an overall policy, I</p> <p>49:8 believe there was one from 2005, and a later</p> <p>49:9 one from 2007, an overall policy that was</p> <p>49:10 comprised of a lot of procedures, which I</p> <p>49:11 believe is in the binder.</p> <p>49:12 Q. Okay. You can go ahead and --</p> <p>49:13 feel free to consult the binder. And if you</p> <p>49:14 could point out the policy you're referring</p> <p>49:15 to, that would be great.</p> <p>49:16 A. Sure. If you turn to Tab 4L.</p> <p>49:17 Q. Yes.</p> <p>49:18 A. So this is the overall policy</p> <p>49:19 which I said is composed of several</p> <p>49:20 procedures.</p> <p>49:21 Q. Now, the index indicates that</p> <p>49:22 Tab 4L is dated December 17, 2007?</p> <p>49:23 A. Is that a question? I'm sorry.</p> <p>49:24 Q. Yes. Do you see that?</p>

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**Kenneweg**  
**30(b)(6) Tr. at**  
**52:22-55:19**

52:22 Q. Yes. Were AMO reviews  
 52:23 conducted on originators whose loans backed  
 52:24 PLS securities?

53:3 A. Yes.

53:4 Q. And in those reviews what  
 53:5 information was considered by AMO?

53:6 A. Credit guidelines. I mean,  
 53:7 there were a number of different categories,  
 53:8 but at a high level my recollection is credit  
 53:9 guidelines. Quality control. Compliance.  
 53:10 Overall controls at the company. So, you  
 53:11 know, sometimes it probably varied, depending  
 53:12 on the exact business model of the  
 53:13 counterparty. But at a high level those were  
 53:14 some of the topics.

53:15 Q. When you say "credit  
 53:16 guidelines," do you mean underwriting  
 53:17 guidelines?

53:18 A. Yes.

53:19 Q. And did the AMO reviews involve  
 53:20 loan-level review?

53:22 A. What type of AMO reviews?

53:23 Q. Of originators.

53:24 A. Yes.

53:25 Q. And was the purpose of the

54:2 review, among other things, speaking again of  
 54:3 originators, to determine the originators'  
 54:4 compliance with their underwriting guidelines?

54:6 A. My understanding was the  
 54:7 reviews were not to serve so much as an audit  
 54:8 on their compliance; it was more to get an  
 54:9 understanding of the riskiness of their  
 54:10 guidelines, and to get a sense for the types  
 54:11 of loans they were underwriting.

54:12 Q. And whether or not those loans  
 54:13 were of poor credit quality?

54:15 A. Um, not just of poor credit  
 54:16 quality, but to be able to provide an



<b>GSE Counterparty Reviews and Policies</b>	
	<p>54:17 assessment of the average loan quality.  54:18 Q. And to determine whether or not  54:19 the documentation in the loan file was  54:20 consistent with what Freddie Mac expected?</p> <p>54:22 BY MR. SECHLER:  54:23 Q. Right?  54:24 A. I am -- I'm not sure about that  54:25 specifically.</p> <p>55:2 Q. To identify concerns with the  55:3 originators' underwriting processes?</p> <p>55:5 A. That's, again, very specific.  55:6 Q. What do you mean, that's very  55:7 specific?  55:8 A. I didn't actually attend the  55:9 loan file reviews, so your questions are about  55:10 the loan file reviews.  55:11 Q. But you read the AMO  55:12 operational reviews, didn't you?  55:13 A. I did. And I attended one of  55:14 the onsite management meetings. One of the  55:15 portions, yes.  55:16 Q. How many AMO operational  55:17 reviews did you review between 2005 and 2007?</p> <p>55:19 A. I didn't count.</p>
<b>Kenneweg 30(b)(6) Tr. at 58:16-59:6</b>	<p>58:16 A. It's an origination operation  58:17 review of First NLC's Financial Services.  58:18 Q. That's the attachment to the  58:19 e-mail?  58:20 A. The attachment is the review  58:21 memo.  58:22 Q. And the e-mail was sent out by  58:23 Mary Joe Whipple. Is that right?  58:24 A. Yes.  58:25 Q. On or about June 16, 2006.</p> <p>59:2 Right?  59:3 A. Yes.  59:4 Q. And you were one of the  59:5 recipients. Correct?</p>

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	59:6 A. I was, mm-hmm.
<b>Kenneweg 30(b)(6) Tr. at 59:11-19</b>	<p>59:11 Q. Is this review an example of 59:12 the kinds of reviews that AMO did of 59:13 originators whose loans backed PLS?</p> <p>59:16 A. This looks consistent with the 59:17 type of review that AMO completed.</p> <p>59:18 Q. Now, do you see in this 59:19 distribution list the name Mike Aneiro?</p>
<b>Kenneweg 30(b)(6) Tr. at 182:11-20</b>	<p>182:11 Ms. Kenneweg, can you tell me 182:12 what the second attachment to your e-mail is?</p> <p>182:13 A. This is the originators, 182:14 servicers and conduits scorecard.</p> <p>182:15 Q. And was this something that was 182:16 circulated on a monthly basis?</p> <p>182:17 A. I can't recall if it was 182:18 monthly or quarterly.</p> <p>182:19 Q. And who circulated this?</p> <p>182:20 A. I would have.</p>
<b>Kenneweg 30(b)(6) Tr. at 183:4-19</b>	<p>183:4 Q. And to whom did you distribute 183:5 these scorecards?</p> <p>183:6 A. I don't recall the entire 183:7 distribution list, but the portfolio managers 183:8 would have received it, and PM&amp;P, and CCR 183:9 management.</p> <p>183:10 Q. And when you say the portfolio 183:11 managers, do you mean the traders?</p> <p>183:12 A. Yes.</p> <p>183:13 Q. And the PM&amp;P group including 183:14 Mr. Palmer?</p> <p>183:15 A. Yes.</p> <p>183:16 Q. And these scorecards reflect 183:17 the metrix scores that CCRM has assigned to 183:18 originator counterparties, correct?</p> <p>183:19 A. That's correct.</p>
<b>Kenneweg 30(b)(6) Tr. at 211:18 – 212:19</b>	<p>211:18 Q. Yes. Why did Freddie Mac have 211:19 the policy that an operational review was not 211:20 required for assigning a metrix score to an 211:21 originator at the AAA investment level?</p> <p>211:24 A. Well, I mean, an overall 211:25 comment -- you know, it would be impractical</p>

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	<p>212:2 to assign an operational review to every 212:3 single originator on the list, so...</p> <p>...</p> <p>212:6 A. No. I was just going to say it 212:7 wouldn't be feasible to go onsite and do an 212:8 operational review of every single originator.</p> <p>212:9 Q. Well, wasn't approval only 212:10 required for originators whose loans 212:11 constituted more than 1 percent of the unpaid 212:12 principal balance?</p> <p>212:13 A. That's right.</p> <p>212:14 Q. And even within that subset of 212:15 originators whose loans constitute more than 1 212:16 percent of the unpaid principal balance, if 212:17 they were originators at the AAA investment 212:18 level you didn't need an operational review, 212:19 would you?</p>
<b>Kenneweg 30(b)(6) Tr. at 212:24 – 214:10</b>	<p>212:24 Q. You wouldn't need an 212:25 operational review of an originator whose</p> <p>213:2 loans constituted more than 1 percent of the 213:3 unpaid principal balance under this policy, 213:4 would you?</p> <p>213:7 A. I don't think I agree with 213:8 that.</p> <p>213:9 Q. Okay. Why don't you agree with 213:10 that?</p> <p>213:11 A. That an originator does not 213:12 need an operational review if they had above 1 213:13 percent.</p> <p>213:14 Q. Okay. So an originator -- any 213:15 originator above 1 percent needed an 213:16 operational review?</p> <p>213:17 A. That's my -- yes. That's my 213:18 understanding.</p> <p>213:19 Q. Okay. And needed to be 213:20 approved by counterparty credit risk 213:21 management?</p> <p>213:22 A. Yes.</p> <p>213:23 Q. And would be assigned a metrix 213:24 score?</p> <p>213:25 A. Yes.</p>

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	<p>214:2 Q. Under what circumstances would  214:3 counterparty credit risk management assign  214:4 metrix scores and approve originators whose  214:5 loans were less than 1 percent of the unpaid  214:6 principal balance?</p> <p>214:9 A. There were not particular  214:10 circumstances.</p>
<b>Kenneweg  30(b)(6) Tr. at  214:18 – 216:17</b>	<p>214:18 Q. Was there any requirement that  214:19 an originator whose loans constituted less  214:20 than 1 percent of the unpaid principal balance  214:21 be approved by CCRM?</p> <p>214:22 A. In the PLS space?</p> <p>214:23 Q. Yes.</p> <p>214:24 A. No. If it was less than 1  214:25 percent, that was not a requirement.</p> <p>215:2 Q. And this policy relates to PLS,  215:3 doesn't it?</p> <p>215:4 A. It does.</p> <p>215:5 Q. Under what circumstances would  215:6 CCRM assign a metrix score to an originator  215:7 whose loans constituted less than 1 percent of  215:8 the unpaid principal balance of Freddie's  215:9 portfolio?</p> <p>215:10 A. If they were already doing  215:11 business with another part of Freddie Mac and  215:12 had a score assigned through that exposure,  215:13 then they would have already had a score  215:14 assigned.</p> <p>215:15 Q. Okay. But apart from having a  215:16 score assigned by having done single-family  215:17 business, was there any requirement that CCRM  215:18 assign a metrix score to PLS counterparties  215:19 who were originators with less than 1 percent  215:20 UPB?</p> <p>215:22 A. I don't believe the MABS  215:23 procedure had any such requirement.</p> <p>215:24 Q. So then what is the relevance  215:25 and application of this sentence in the last</p>

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	<p>216:2 part of this paragraph here, that says, quote,  216:3 "An operational review is not required for  216:4 assigning a metrix score for an originator  216:5 pursuant to PM&amp;P 101 at the AAA investment  216:6 level"?</p> <p>216:9 A. My interpretation of that is,  216:10 in contrast to the first sentence there where  216:11 it says "There must be an operational review  216:12 for any aggregator," that's required for an  216:13 aggregator. In contrast, you don't need it  216:14 automatically to assign a metrix score to an  216:15 originator. It's only once exposure to the  216:16 originator is above 1 percent that you would  216:17 need to conduct an operational review.</p>
<b>Kenneweg 30(b)(6) Tr. at 217:17 – 218:20</b>	<p>217:17 Originators in the PLS space  217:18 would have to be re-reviewed on a periodic  217:19 basis under procedure 123?  217:20 A. Correct.  217:21 Q. How often?  217:22 A. According to this procedure,  217:23 every 24 months.  217:24 Q. And again, that only applies to  217:25 originators whose loans constitute more than 1</p> <p>218:2 percent of the unpaid principal balance?  218:3 A. Correct.  218:4 Q. And then apart from the  218:5 above-1-percent gang you also had special  218:6 reviews of the top ten originators?  218:7 A. Correct.  218:8 Q. And were those a different kind  218:9 of review?  218:10 A. Yes. So those were a writeup,  218:11 more of a full analysis, versus the  218:12 seller/servicers just received an automatic --  218:13 an automated score, calculation. So that the  218:14 top ten was a bit of a deeper dive.  218:15 Q. And the deeper dive was called  218:16 a high profile counterparty review?  218:17 A. Correct.  218:18 Q. And there's an example of that  218:19 attached as Appendix D, is that correct?</p>

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	218:20 A. Yes.
<b>Kenneweg 30(b)(6) Tr. at 238:25 – 239:15</b>	<p>238:25 Q. Do you have any reason to</p> <p>239:2 believe this was not a monthly scorecard?</p> <p>239:4 A. I don't.</p> <p>239:5 Q. But as you sit here today as a</p> <p>239:6 30(b)(6) designee you don't know with what</p> <p>239:7 frequency these scorecards were generated by</p> <p>239:8 AMO?</p> <p>239:11 A. We could refer to their</p> <p>239:12 procedures to see if they specify in there. I</p> <p>239:13 mean, this is labeled August, but I don't</p> <p>239:14 recall the exact frequency with which they</p> <p>239:15 distributed a certain report.</p>
<b>Kenneweg 30(b)(6) Tr. at 239:20 – 240:11</b>	<p>239:20 Q. Which operational reviews would</p> <p>239:21 be shown in the scorecard?</p> <p>239:22 A. I believe their format -- is it</p> <p>239:23 back here? I believe they had -- yeah, they</p> <p>239:24 had different columns. I mean, they'll show,</p> <p>239:25 I believe, all the counterparties that they</p> <p>240:2 might have reviewed -- that AMO might have</p> <p>240:3 reviewed.</p> <p>240:4 Q. Over a given period, or ever?</p> <p>240:7 A. I don't know at what point they</p> <p>240:8 might have removed counterparties.</p> <p>240:9 Q. Okay.</p> <p>240:10 A. I mean, certainly they -- they</p> <p>240:11 noted if some were inactive. But...</p>
<b>Kenneweg 30(b)(6) Tr. at 240:15 – 242:9</b>	<p>240:15 What was the purpose of this</p> <p>240:16 AMO scorecard?</p> <p>240:17 A. To summarize AMO's assessment</p> <p>240:18 of a counterparty's business model and the</p> <p>240:19 risks inherent in the business model.</p> <p>240:20 Q. And is it your understanding</p> <p>240:21 that a score of 4 in the areas of credit</p> <p>240:22 appraisal, management or controls is a poor</p> <p>240:23 score?</p> <p>240:24 A. It's been so long since I have</p> <p>240:25 looked -- you know, used -- used these to that</p>

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	<p>241:2 level of detail. But, I mean, we could refer  241:3 to the bottom table on here.  241:4 Q. Okay. Do you see it says -- go  241:5 ahead.  241:6 A. Yeah, that would indicate 3.8  241:7 or greater.  241:8 Q. And what does 3.8 or greater  241:9 mean?  241:10 A. "Does not meet minimum  241:11 competencies or has critical control  241:12 weaknesses."  241:13 Q. Do you see there are a number  241:14 of originators here in this scorecard  241:15 circulated in September of 2007 who, in the  241:16 credit area, did not meet minimum competencies  241:17 or had critical control weaknesses?</p> <p>241:20 A. It looks like there were a few  241:21 that were rated a 4 in that category.  241:22 Q. And do you see there also are  241:23 originators indicated on this scorecard that  241:24 in the appraisal area did not meet minimum  241:25 competencies or had critical control</p> <p>242:2 weaknesses?</p> <p>242:4 A. I do see there were a few that  242:5 received scores of 4.  242:6 Q. And in fact if you look at  242:7 Argent, Argent received a score of 4 in both  242:8 the credit and appraisal areas, is that right?  242:9 A. That's right.</p>
<b>Kenneweg Tr. at 51:8 – 54:24</b>	<p>51:8 Q. Okay. When I refer to "AMO," I'm  51:9 referring to the alternative markets  51:10 operations, right?  51:11 A. Right.  51:12 Q. Okay. Is it fair to say that CCRM  51:13 would be more cautious of counterparties with  51:14 poor controls than it would be of  51:15 counterparties who had excellent controls?</p> <p>51:17 THE WITNESS: We had similar -- we  51:18 had a pretty consistent framework, pretty</p>

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51:19 consistent process, so I don't -- what did you  
51:20 say, we would be more cautious of?  
51:21 I would say it was a consideration  
51:22 in our -- in our evaluation.  
51:23 BY MR. COHEN:  
51:24 Q. Sure.  
51:25 All right. Let's move on to Page  
  
52:2 6540, which is titled "Metrix Framework."  
52:3 Do you see that?  
52:4 A. I do.  
52:5 Q. And this chart, essentially,  
52:6 describes and explains the meaning of CCRM's  
52:7 Metrix scores which were given to Freddie Mac's  
52:8 various PLS counterparties, right?  
  
52:10 THE WITNESS: Right.  
52:11 BY MR. COHEN:  
52:12 Q. And the Metrix scores represented  
52:13 CCRM's analysis of a counterparty's financial  
52:14 health, right?  
  
52:16 THE WITNESS: Yes.  
52:17 BY MR. COHEN:  
52:18 Q. Okay. And the Metrix risk grades  
52:19 were on a 1 to 20 scale, right, which is in the  
52:20 column -- which is indicated by the column  
52:21 entitled "Risk Grade," right?  
52:22 A. Right.  
52:23 Q. Okay. And then on the second column  
52:24 from the left it says, "Risk Segment," and  
52:25 the -- essentially, the Metrix scores were  
  
53:2 further segmented on M1 through M7 scale,  
53:3 right?  
  
53:5 THE WITNESS: Right.  
53:6 BY MR. COHEN:  
53:7 Q. Okay. And then the Metrix scores  
53:8 were also tied to external rating agency  
53:9 equivalence, right?  
53:10 A. Right.  
53:11 Q. Okay. Let's turn to Page 6543,



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	53:12	which at the top of the page states: "CCRM
	53:13	surveillance process."
	53:14	Do you see that?
	53:15	A. I do.
	53:16	Q. Okay. And then fourth bullet --
	53:17	excuse me -- fourth bullet from the bottom, it
	53:18	states: "Mortgage ABS, review of major
	53:19	issuers, originators, servicers annually."
	53:20	Do you see that?
	53:21	A. I do.
	53:22	Q. So that was one of your job
	53:23	functions during the 2005 to 2007 time period,
	53:24	right?
	53:25	A. Right.
	54:2	Q. And CCRM performed annual reviews of
	54:3	mortgage -- MABS counterparties, right?
	54:5	THE WITNESS: Right.
	54:6	BY MR. COHEN:
	54:7	Q. But CCRM also performed ongoing
	54:8	surveillance of MABS counterparties, right? It
	54:9	wasn't just that you look at them once a year
	54:10	and then you don't look at them until a year
	54:11	from then, right?
	54:12	A. That's right.
	54:13	Q. Okay. How did CCRM perform ongoing
	54:14	surveillance of Freddie Mac's MABS
	54:15	counterparties?
	54:16	A. Well, there might have been ad hoc
	54:17	requests. There was exposure reporting where
	54:18	we would constantly monitor the outstanding
	54:19	exposure versus the limits that had been set.
	54:20	Just staying abreast of news.
	54:21	Q. You also measured the concentration
	54:22	of a given a counterparties' production and
	54:23	Freddie Mac's MABS portfolio, too, right?
	54:24	A. That's right.
<b>Kenneweg Tr. at 55:9 – 55:25</b>	55:9	Q. Yeah. Sorry about that.
	55:10	Part of the ongoing surveillance
	55:11	function also required you to basically stay up
	55:12	on what was going on in the market, right?
	55:13	A. At a high level, yes.

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	55:14	Q. Sure.
	55:15	Is it fair to say that during the
	55:16	2005 to 2007 time period, CCRM was primarily
	55:17	responsible for surveillance of Freddie Mac's
	55:18	counterparties and the CPPM organization was
	55:19	responsible for surveillance of bonds that
	55:20	Freddie Mac had purchased?
	55:22	THE WITNESS: I would say CCRM was
	55:23	responsible for monitoring the counterparties.
	55:24	I probably shouldn't speak to other
	55:25	organizations' responsibilities.
<b>Kenneweg Tr. at 59:7 – 59:18</b>	59:7	Q. Okay. Let's turn to Page 6551.
	59:8	Reasons for termination -- and I'm going to --
	59:9	not paraphrase, but not read all of them.
	59:10	"Some of the primary reasons for terminations
	59:11	are "Poor audit findings, EORM, poor loan
	59:12	quality, QC, fraud, FIU."
	59:13	Do you see that?
	59:14	A. I do.
	59:15	Q. The reference to EORM is a reference
	59:16	to Freddie Mac's external operations risk
	59:17	management organization, correct?
	59:18	A. Yes.
<b>Kenneweg Tr. at 60:3 – 61:5</b>	60:3	Q. Okay. But did you understand that
	60:4	EORM audited Freddie Mac's counterparties, as
	60:5	it says here?
	60:7	THE WITNESS: They conducted
	60:8	operational reviews.
	60:9	BY MR. COHEN:
	60:10	Q. Okay. And sometimes they found, as
	60:11	it suggests here, that some of those -- that
	60:12	some of Freddie Mac's counterparties had a poor
	60:13	business practice, correct?
	60:15	THE WITNESS: I don't think this
	60:16	document says that. I think it says that's a
	60:17	potential reason for termination.
	60:18	BY MR. COHEN:
	60:19	Q. Okay. And it similarly says that a
	60:20	potential reason for termination is poor loan
	60:21	qualities as determined by Freddie Mac's QC or

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	<p>60:22 quality control organization, right?</p> <p>60:23 A. I don't think the document says</p> <p>60:24 necessarily coming from that part of the</p> <p>60:25 organization. It just says, "poor loan</p> <p>61:2 quality."</p> <p>61:3 Q. What do you understand the reference</p> <p>61:4 to QC to mean?</p> <p>61:5 A. Quality control.</p>
<b>Kenneweg Tr. at 66:15 – 67:11</b>	<p>66:15 How did CCRM receive information</p> <p>66:16 from the PLS business units regarding the</p> <p>66:17 credit quality of Freddie Mac's PLS</p> <p>66:18 counterparties?</p> <p>66:20 THE WITNESS: The credit quality of</p> <p>66:21 our counterparties?</p> <p>66:22 BY MR. COHEN:</p> <p>66:23 Q. Yes.</p> <p>66:24 A. I was responsible for monitoring</p> <p>66:25 their financial statements, so I was</p> <p>67:2 responsible for assessing credit quality of the</p> <p>67:3 counterparties.</p> <p>67:5 And how did you get that information</p> <p>67:6 from the PLS business units?</p> <p>67:8 THE WITNESS: They did not supply me</p> <p>67:9 with counterparty financial information. I was</p> <p>67:10 responsible for obtaining the financial</p> <p>67:11 statements, analyzing the financial statements.</p>
<b>Kenneweg Tr. at 76:2 – 76:14</b>	<p>76:2 Q. Okay. In the second -- strike that.</p> <p>76:3 In the bottom most bubble it states</p> <p>76:4 in the second bullet point that "CCRM's role is</p> <p>76:5 to ensure that I&amp;CM 'transacts only with</p> <p>76:6 counterparties/issuers whose credit risks are</p> <p>76:7 understood and quantified.'"</p> <p>76:8 Do you see that?</p> <p>76:10 THE WITNESS: I do.</p> <p>76:11 BY MR. COHEN:</p> <p>76:12 Q. That, too, was one of CCRM's</p> <p>76:13 responsibilities, right?</p>

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	76:14	A. Yes.
Kenneweg Tr. at 76:21 – 79:2	76:21	Q. Sure.
	76:22	Well, in the fourth bullet point in
	76:23	the top most bubble, it says: "Issuer exposure
	76:24	is the economic loss of a security or its
	76:25	issuer are downgraded or defaults."
	77:2	So issuer risk might include the
	77:3	possibility of a security or issuer would be
	77:4	downgraded or default, right?
	77:6	THE WITNESS: We monitor issuers and
	77:7	their creditworthiness.
	77:8	BY MR. COHEN:
	77:10	And you monitored all other kinds of
	77:11	counterparties, too, right?
	77:13	THE WITNESS: Not all other kinds,
	77:14	but we monitored some other kinds.
	77:15	BY MR. COHEN:
	77:17	But the originators of subprime
	77:18	loans, right?
	77:20	THE WITNESS: Our PLS originator
	77:21	counterparties, yes.
	77:22	BY MR. COHEN:
	77:25	How did you get information to
	78:2	understand and quantify the credit risk of
	78:3	Freddie Mac's PLS counterparties?
	78:5	THE WITNESS: Depended on the -- I
	78:6	guess depended on the situation. Sometimes
	78:7	financials would be available through public
	78:8	means like SEC's website. Sometimes we would
	78:9	have to reach out to the counterparty and ask
	78:10	them if they didn't have public financials.
	78:11	BY MR. COHEN:
	78:13	Would AMO reports also provide you

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	78:14	information on the credit risk of
	78:15	counterparties?
	78:17	THE WITNESS: Not the financial
	78:18	condition, necessarily. It was just another
	78:19	piece of information.
	78:20	BY MR. COHEN:
	78:21	Q. Which was relevant to the riskiness
	78:22	of the counterparty, right?
	78:24	THE WITNESS: It would inform your
	78:25	overall assessment of the -- of the
	79:2	creditworthiness of the counterparty.
<b>Kenneweg Tr. at 80:9 – 81:16</b>	80:9	Q. Okay. Ms. Kenneweg, let me show you
	80:10	another document which is Bates No. FHFA
	80:11	01485802. And this has already been introduced
	80:12	as Exhibit 1834, I believe, at your 30(b)(6)
	80:13	deposition.
	80:14	Do you recognize this document?
	80:15	A. Yes.
	80:16	Q. Is it fair to say that this was the
	80:17	main departmental policy governing the
	80:18	activities of counterparty credit risk
	80:19	management within Freddie Mac's capital markets
	80:20	division?
	80:21	A. Yes.
	80:22	Q. Okay. On the first page at -- which
	80:23	is No. 5802, the fifth bullet point from the
	80:24	bottom states that "One of CCRM's
	80:25	responsibilities was to 'provide for
	81:2	consistency with industry best practices and
	81:3	regulatory expectations."
	81:4	Do you see that?
	81:5	A. Yes.
	81:6	Q. What do you understand the term
	81:7	"industry best practices" to mean?
	81:8	A. Well, I would say keeping up with --
	81:9	I don't know how to rephrase that.
	81:10	Q. The best practices in the PLS
	81:11	subprime?
	81:12	A. As peers do and -- I'm trying to

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	81:13	define it without giving examples, but, you
	81:14	know, just keeping up with -- I guess with
	81:15	controls and processes that other people in the
	81:16	industry might -- might have.
<b>Kenneweg Tr. at 97:12 – 99:13</b>	97:12	Q. Ms. Kenneweg, I would like to show
	97:13	you another document which has previously been
	97:14	marked as Exhibit 1825. And that is Bates No.
	97:15	FHFA 11950446.
	97:19	The first page of this document is a
	97:20	December 10, 2009 e-mail from you to Karen
	97:21	Gifford, correct?
	97:22	A. It appears so.
	97:23	Q. And it appears that you attached
	97:24	the: "MABS counterparty procedure," right?
	97:25	A. It looks like it.
	98:2	Q. Okay. Let's turn to Page 0450.
	98:3	Ms. Kenneweg, do you recognize this
	98:4	document?
	98:5	A. Yes.
	98:9	"This procedure outlines the process
	98:10	for reviewing and approving new mortgage ABS
	98:11	counterparties as well as ongoing monitoring of
	98:12	existing counterparties."
	98:13	Do you see that?
	98:14	A. I see it.
	98:15	Q. Is it fair to say this procedure
	98:16	provided the framework for your approval of new
	98:17	PLS counterparties?
	98:19	THE WITNESS: Well, you changed the
	98:20	wording a little bit. According to this
	98:21	procedure, it outlines the process for
	98:22	reviewing and approving.
	98:23	BY MR. COHEN:
	98:24	Q. Okay. And it's fair to say this
	98:25	procedure also outlines a process for ongoing
	99:2	monitoring of existing counterparties, right?
	99:3	A. That is what it says, yes.
	99:4	Q. Which ongoing monitoring could also

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	99:5	be called surveillance of existing PLS
	99:6	counterparties, right?
	99:8	THE WITNESS: Yes.
	99:9	BY MR. COHEN:
	99:10	Q. What other procedures did CCRM use
	99:11	for this function?
	99:13	THE WITNESS: I don't know.
<b>Kenneweg Tr. at 107:4 – 107:10</b>	107:4	Q. Okay. Let's turn back to the
	107:5	procedure.
	107:6	At the top of the page ending in
	107:7	0451, potential new MABS counterparties:
	107:8	"Counterparties will require approval pursuant
	107:9	to the thresholds described in the counterparty
	107:10	approval Metrix."
<b>Kenneweg Tr. at 107:19 – 108:2</b>	107:19	A. Okay.
	107:20	Q. And below that it says: "For
	107:21	issuers, the MABS trading desk or structured
	107:22	credit notifies CCRM of potential applicant."
	107:23	Do you see that?
	107:24	A. I do.
	107:25	Q. Is this consistent with your
	108:2	experiencing during 2005, 2007?
<b>Kenneweg Tr. at 108:15 – 110:6</b>	108:15	So CCRM was generally informed by
	108:16	the PLS desk in Kevin Palmer and Frank
	108:17	Vitrano's group about potential new issuers of
	108:18	private label securities, right?
	108:20	THE WITNESS: That is what this
	108:21	document says, yes.
	108:22	BY MR. COHEN:
	108:23	Q. Is that consistent with your
	108:24	recollection?
	108:25	A. Yes.
	109:2	Q. How was CCRM informed about other
	109:3	potential new PLS counterparties, nonissuers?
	109:4	A. I think it depends on the situation.
	109:5	I mean, sometimes it would be consistent with
	109:6	that bullet where the traders or someone, you
	109:7	know, Kevin's organization might approach us if

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	109:8	it was a counterparty that they didn't see on,
	109:9	you know, one of our lists.
	109:10	Or it is possible that exposure was
	109:11	getting up to a certain point where it might
	109:12	hit a threshold where we would start monitoring
	109:13	so, you know, I guess there is a couple of
	109:14	different ways they could appear on our radar.
	109:15	Q. Do you remember any other Freddie
	109:16	Mac organizations informing CCRM about new
	109:17	nonissuer counterparties?
	109:18	A. For the PLS sector, no.
	109:19	Q. Okay. So it's fair to say you would
	109:20	either be informed by the MABS desk, Kevin
	109:21	Palmer's group, or they would come to your
	109:22	attention because of Freddie Mac's increasing
	109:23	exposure of concentrations to the counterparty,
	109:24	right?
	110:2	THE WITNESS: Those are the ones
	110:3	that I can recall right now. I'm not saying it
	110:4	is not possible. There might have been some
	110:5	other means, but that's what I remember right
	110:6	now.
<b>Kenneweg Tr. at 111:22 – 112:5</b>	111:22	Q. The next bullet states that: "A
	111:23	comprehensive review of the financial data is
	111:24	performed with consideration given to" -- and
	111:25	then it goes on to list a number of factors.
	112:2	The bottom factors are: "Delivery volume,
	112:3	process controls and business models."
	112:4	Do you see that?
	112:5	A. I do.
<b>Kenneweg Tr. at 117:11 – 117:15</b>	117:11	It says here that CCRM performed a
	117:12	comprehensive review of the financial data with
	117:13	consideration given to, among other things,
	117:14	process controls, right?
	117:15	A. Uh-huh. Yes.
<b>Kenneweg Tr. at 117:18 – 118:2</b>	117:18	You would have considered the
	117:19	counterparty's process controls in determining
	117:20	whether to approve a counterparty for business
	117:21	with Freddie Mac, right?
	117:23	THE WITNESS: I don't know. You're
	117:24	focusing on two words within a procedure from



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	<p>117:25 many years ago, so I am not going to be able to</p> <p>118:2 give you detail about those two words.</p>
<b>Kenneweg Tr. at 121:2 – 121:5</b>	<p>121:2 Q. Do you remember preparing written</p> <p>121:3 reviews of potential MABS counterparties?</p> <p>121:4 A. I prepared written reviews. I don't</p> <p>121:5 remember writing the reviews.</p>
<b>Kenneweg Tr. at 122:17 – 125:4</b>	<p>122:17 Q. It states: "Guidelines generally</p> <p>122:18 applied that determine the approximate</p> <p>122:19 creditworthiness of a counterparty are," and it</p> <p>122:20 goes on to list a couple of things.</p> <p>122:21 In the third bullet point, it states</p> <p>122:22 that: "Poor operational review would be</p> <p>122:23 considered."</p> <p>123:2 Q. Do you see that?</p> <p>123:3 A. I do.</p> <p>123:4 Q. Is that a reference to AMO reviews?</p> <p>123:5 A. The operational review --</p> <p>123:6 Q. Yes.</p> <p>123:7 A. -- words? Yes.</p> <p>...</p> <p>123:9 So it is fair to say that CCRM would</p> <p>123:10 consider AMO's reviews in assigning Metrix</p> <p>123:11 scores, right?</p> <p>123:12 A. Yes.</p> <p>123:13 Q. Okay. Next bullet point: "These</p> <p>123:14 guidelines are not absolute criteria for</p> <p>123:15 assigning individual category scores as</p> <p>123:16 subjective measures such as loan quality,</p> <p>123:17 diversification, parental strength and other</p> <p>123:18 factors are considered."</p> <p>123:19 Do you see that?</p> <p>123:20 A. I do.</p> <p>123:21 Q. It says that: "CCRM considered loan</p> <p>123:22 quality in applying the Metrix framework,"</p> <p>123:23 right?</p> <p>123:24 A. Yes.</p> <p>123:25 Q. How did CCRM determine loan quality</p> <p>124:2 in assigning Metrix scores?</p> <p>124:3 A. I don't recall.</p> <p>124:4 Q. What sources of information might</p>

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	124:5	CCRM have considered in determining loan
	124:6	quality of Freddie Mac's PLS counterparties?
	124:7	A. A lot of the -- I believe that there
	124:8	were certain high level, I guess,
	124:9	stratification of either a portfolio the
	124:10	company might have retained or their
	124:11	origination practices a lot of times in the
	124:12	10-Q or 10-K.
	124:13	Also in some of the investor, you
	124:14	know, the marketing materials, they would
	124:15	present their, I guess, typical loan quality
	124:16	Metrix.
	124:17	Q. AMO's reviews also discussed loan
	124:18	quality, right?
	124:20	THE WITNESS: I don't know if I
	124:21	would phrase it like that.
	124:22	BY MR. COHEN:
	124:23	Q. How would you phrase it?
	124:25	THE WITNESS: I would say it was a
	125:2	review of their operations and controls. I
	125:3	just don't know that I would be so specific to
	125:4	say they reviewed loan quality.
<b>Kenneweg Tr. at 127:12 – 128:22</b>	127:12	Q. What was your understanding in 2005
	127:13	to 2007 of why AMO reviewed a sample of loans?
	127:14	A. I don't really want to speculate on
	127:15	why AMO did what they did as part of their
	127:16	process. I was a user of the final report and
	127:17	the final rating, but I don't want to
	127:18	hypothesize on why they did what they did.
	127:19	Q. As a user of the report, what is
	127:20	your understanding of the purpose of the
	127:21	report?
	127:22	A. Just to help inform our overall
	127:23	assessment of the counterparty.
	127:24	Q. And the sampling was part of that,
	127:25	right?
	128:3	THE WITNESS: In some reviews, they
	128:4	did do a sample of loan review, yes.
	128:5	BY MR. COHEN:

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	<p>128:6 Q. And that helped inform your 128:7 subjective application of a measure like loan 128:8 quality, right?</p> <p>128:10 THE WITNESS: I wouldn't say their 128:11 specific loan review helped inform my decision. 128:12 I would say their overall assessment and their 128:13 rating helped inform. It was one piece of 128:14 information I considered.</p> <p>128:15 BY MR. COHEN:</p> <p>128:16 Q. So is it fair to say that you 128:17 reviewed AMO's review of loan quality in -- or 128:18 assessment of the counterparty's financial 128:19 health?</p> <p>128:21 THE WITNESS: I considered AMO's 128:22 overall report.</p>
<b>Kenneweg Tr. at 130:14 – 131:21</b>	<p>130:14 Q. In the next paragraph down, it 130:15 states that: "Completion of an operational 130:16 review is required for all aggregators for 130:17 approval and to assign the Metrix score. 130:18 Because assessment of an aggregator's processes 130:19 and controls is essential to ensuring 130:20 appropriate loan quality, the operational 130:21 review is a key component in assessing 130:22 counterparty risk for this group." 130:23 Do you see that?</p> <p>130:24 A. I do.</p> <p>130:25 Q. What kind of things did CCRM look</p> <p>131:2 for in reviewing an aggregator's processes?</p> <p>131:3 A. CCRM didn't necessarily assess all 131:4 the processes. We would have relied on an 131:5 operational review for that purpose.</p> <p>131:6 Q. What kind of things did CCRM look 131:7 for in assessing an aggregator's controls?</p> <p>131:8 A. I don't recall.</p> <p>131:9 Q. The next sentence states: "An 131:10 operational review is not required for 131:11 assigning a Metrix score for an originator 131:12 pursuant to PM&amp;P 101, the Triple A investment 131:13 level." 131:14 Why was an operational review a key</p>

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	131:15	component for ensuring loan quality for
	131:16	aggregators and not originators?
	131:18	THE WITNESS: Because we relied on
	131:19	the aggregator to perform due diligence on the
	131:20	loans that they were buying and putting into
	131:21	deals. They are an added layer of protection.
<b>Kenneweg Tr. at 145:5 – 146:9</b>	145:5	Q. At Page 0453, next page, under the
	145:6	second header, it states that: "Periodic
	145:7	meetings are held between all critical parties
	145:8	involved in the MABS counterparty management
	145:9	process. These parties include CCRM, portfolio
	145:10	management, structured credit, AMO and
	145:11	single-family credit management. These
	145:12	meetings are extremely useful in terms of
	145:13	sharing information, such as operational review
	145:14	findings and current events, and also for
	145:15	conveying business area priorities in terms of
	145:16	counterparty activity and review requests.
	145:17	Information gathered at these meetings may aid
	145:18	CCRM in reviewing and rating a counterparty.
	145:19	Additionally, CCRM conveys any recent
	145:20	counterparty score changes at this meeting.
	145:21	These meetings are generally held monthly."
	145:22	Do you see that?
	145:23	A. I do.
	145:24	Q. Do you remember these counterparty
	145:25	form meetings?
	146:2	A. I remember that we had several, yes.
	146:3	Q. Was CCRM responsible for arranging
	146:4	the meetings?
	146:5	A. I believe so, yes.
	146:6	Q. Was it responsible for creating an
	146:7	agenda?
	146:8	A. I believe I usually created the
	146:9	agenda.
<b>Kenneweg Tr. at 239:24 – 240:22</b>	239:24	Q. If you flip to the page ending in
	239:25	Bates No. 451, there is a list of --
	240:2	"Comprehensive review of financial data
	240:3	performed with consideration to," and there is
	240:4	a list of items.
	240:5	Do you recall that?

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	<p>240:6 And one of those items is "process 240:7 controls." 240:8 Do you see that? 240:9 A. I do. 240:10 Q. Did -- was the AMO review part of 240:11 Freddie Mac's procedure for monitoring process 240:12 controls at counterparties?</p> <p>240:14 THE WITNESS: It's -- like I said 240:15 before, I don't recall exactly the context 240:16 between these two words on this overall 240:17 procedure. 240:18 I can tell you the operational 240:19 review is something that we consumed as part of 240:20 our review, but, you know, the meaning behind 240:21 this one bullet point, I'm not sure at this 240:22 point.</p>	
<b>Kenneweg Tr. at 241:11 – 241:23</b>	<p>241:11 Q. How did the operational reviews 241:12 affect your assessment of the financial 241:13 wherewithal of Freddie Mac counterparties?</p> <p>241:15 THE WITNESS: I would say they could 241:16 have impacted the overall rating. I mean, they 241:17 wouldn't necessarily impact this -- how did you 241:18 put it, the financial view? 241:19 BY MR. BENNETT: 241:20 Q. Financial wherewithal. 241:21 A. I would say they could impact the 241:22 overall rating that we would assign a 241:23 counterparty.</p>	
<b>Kenneweg Tr. at 272:22 – 274:18</b>	<p>272:22 The purpose of sending the AMO team 272:23 out to review an originator was to assess the 272:24 risk that that originator posed to Freddie Mac, 272:25 correct?</p> <p>273:3 THE WITNESS: I guess one type of 273:4 risk, yeah, could pose to Freddie Mac. 273:5 BY MR. BENNETT: 273:6 Q. Okay. And the type of risk was the 273:7 risk relating to the relationship with that 273:8 originator and Freddie Mac's PLS business, 273:9 correct? 273:11 THE WITNESS: The relationship of</p>	

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	<p>273:12 that customer and our PLS business?</p> <p>273:13 BY MR. BENNETT:</p> <p>273:14 Q. Yes.</p> <p>273:15 The reason they were -- the</p> <p>273:16 counterparties -- the originators were on the</p> <p>273:17 counterparty list for review is because they</p> <p>273:18 were selling loans into the PLS in which</p> <p>273:19 Freddie was investing?</p> <p>273:20 A. That's correct.</p> <p>273:21 Q. So the goal of the AMO review was to</p> <p>273:22 assess the ways in which that originator</p> <p>273:23 touched the Freddie Mac PLS business?</p> <p>273:25 THE WITNESS: I don't think they</p> <p>274:2 were able to only look at the Freddie Mac PLS</p> <p>274:3 business. It was to assess their overall</p> <p>274:4 processes and controls.</p> <p>274:5 BY MR. BENNETT:</p> <p>274:6 Q. Correct. Correct.</p> <p>274:7 Their overall processes and controls</p> <p>274:8 with the goal of understanding the risk posed</p> <p>274:9 to the Freddie Mac PLS business?</p> <p>274:11 THE WITNESS: That sounds</p> <p>274:12 reasonable.</p> <p>274:13 BY MR. BENNETT:</p> <p>274:14 Q. So they weren't going out, for</p> <p>274:15 example, with the goal of testing policies and</p> <p>274:16 procedures that had nothing to do with Freddie</p> <p>274:17 Mac?</p> <p>274:18 A. Right.</p>
<b>Bates Moss Tr. at 35:19 – 36:11</b>	<p>35:19 Q. What type of counterparties</p> <p>35:20 were reviewed in connection with the</p> <p>35:21 purchase of PLS?</p> <p>35:23 A. Entities that were either</p> <p>35:24 originating, selling or servicing</p> <p>35:25 mortgage products.</p> <p>36:2 Q. What was the purpose of</p> <p>36:3 counterparty reviews?</p> <p>36:4 A. To assess the overall</p>

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	<p>36:5 financial strength of the counterparty  36:6 and its ability to meet its requirements,  36:7 its rep and warrant requirements, and to  36:8 ensure that the counterparties had the  36:9 financial wherewithal and overall  36:10 creditworthiness to do business with  36:11 Fannie Mae.</p>
<b>Bates Moss Tr. at 36:17 – 38:7</b>	<p>36:17 Q. Were there different types of  36:18 counterparty reviews?  36:19 A. Yes.  36:20 Q. What types were there?  36:21 A. There were desk reviews and  36:22 there were onsite reviews.  36:23 Q. What did an onsite review  36:24 consist of?  36:25 A. A team of operational review</p> <p>37:2 analysts would review information --  37:3 review the underwriting, operations,  37:4 origination practices and processes on  37:5 the traditional side relative to the  37:6 seller/servicer guide. They would spend  37:7 time with management to understand sort  37:8 of their entire sort of mortgage  37:9 origination and servicing processes and  37:10 policies. And again, typically, that was  37:11 done relative to the seller/servicer  37:12 guide requirements, we wanted to ensure  37:13 that they were in compliance with such  37:14 requirements.  37:15 Q. Would the same type of onsite  37:16 review occur in connection with  37:17 nontraditional counterparties?  37:18 A. Yes. I mean the focus again  37:19 was trying to ensure that we had a good  37:20 understanding of the overall financial  37:21 capacity and strength of that  37:22 counterparty, and so we would meet with  37:23 management and review with them their  37:24 policies and procedures and processes.  37:25 Q. During your time at Fannie</p>

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	<p>38:2 Mae, can you give an estimate of</p> <p>38:3 approximately how many counterparty</p> <p>38:4 reviews occurred?</p> <p>38:5 A. I would say, while I cannot</p> <p>38:6 recall the specific number, I would -- 70</p> <p>38:7 to 80 such reviews.</p>
<b>Bates Moss Tr. at 39:2 – 41:3</b>	<p>39:2 Q. One of the counterparties</p> <p>39:3 though that your group reviewed was</p> <p>39:4 originators of loans?</p> <p>39:5 A. That's correct.</p> <p>39:6 Q. And how would you determine</p> <p>39:7 which originators to review?</p> <p>39:8 A. Our practice was to review --</p> <p>39:9 to develop a plan to review a certain</p> <p>39:10 number of counterparties on an ongoing</p> <p>39:11 basis. Fannie Mae conducted business</p> <p>39:12 with thousands of counterparties. We set</p> <p>39:13 -- we determined a prioritization review</p> <p>39:14 schedule which included criteria such as</p> <p>39:15 if the counterparty was on a watch list,</p> <p>39:16 if a counterparty, if there was a pending</p> <p>39:17 transaction with the counterparty. If a</p> <p>39:18 counterparty was applying for the first</p> <p>39:19 time to deliver mortgages to Fannie Mae.</p> <p>39:20 Q. Was the volume of Fannie Mae</p> <p>39:21 purchases from a counterparty also a</p> <p>39:22 factor in determining whether to review a</p> <p>39:23 counterparty?</p> <p>39:24 A. Not necessarily.</p> <p>39:25 Q. What type of information would</p> <p>40:2 your counterparty review team obtain</p> <p>40:3 about an originator's origination</p> <p>40:4 processes?</p> <p>40:6 A. We would review their</p> <p>40:7 procedures, their policies, their</p> <p>40:8 processes.</p> <p>40:9 Q. What type of information would</p> <p>40:10 you obtain in a review of a counterparty</p> <p>40:11 with respect to their appraisal</p> <p>40:12 processes?</p>



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	<p>40:15 A. We then would review their  40:16 procurement process and their internal  40:17 procedures and processes and policies  40:18 with respect to selection of appraisers  40:19 and qualifications and such matters.  40:20 Q. Would you undertake to review  40:21 the quality of their appraisal processes?</p> <p>40:24 A. Our focus was on compliance  40:25 relative to Fannie Mae's requirements.</p> <p>41:2 So we focused on ensuring that those  41:3 criteria were in place.</p>
<b>Bates Moss Tr. at 74:5 – 75:20</b>	<p>74:5 Q. Did your group retain Clayton  74:6 to perform onsite operational reviews?  74:7 A. Yes.  74:8 Q. And did that include loan  74:9 level due diligence from time to time?  74:10 A. That included some loan  74:11 sampling, yes.  74:12 Q. And when your employee or  74:13 employees went on site with Clayton,  74:14 would they also be involved in performing  74:15 loan level due diligence of  74:16 counterparties?  74:17 A. From time to time.  74:18 Q. Including of originators?</p> <p>74:20 A. Yes.  74:21 Q. Including originators of  74:22 subprime and Alt-A loans?</p> <p>74:24 A. For the purposes of ensuring  74:25 compliance with the seller/servicer  75:2 guide, yes.  75:3 Q. And you were aware that those  75:4 originators also sold their subprime and  75:5 Alt-A loans into private label  75:6 securities?</p>

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	<p>75:8 A. That could have been the case, 75:9 yes.</p> <p>75:10 Q. What was the operational 75:11 review and compliance group, the acronym 75:12 ORC seems to be associated with it, ORC?</p> <p>75:13 A. It's the group that was 75:14 responsible for going onsite and 75:15 conducting a review of the origination, 75:16 underwriting, servicing, selling, 75:17 policies, procedures, processes of any 75:18 one of those entities.</p> <p>75:19 Q. Were they part of your group?</p> <p>75:20 A. Yes.</p>
<b>Bates Moss Tr. at 76:13 – 77:16</b>	<p>76:13 Q. And you mentioned the legal 76:14 department a few minutes ago. Were they 76:15 also involved in some way in reviewing 76:16 counterparties?</p> <p>76:17 A. Predatory lending.</p> <p>76:18 Q. Was that the sole scope of 76:19 their review, to the best of your 76:20 knowledge?</p> <p>76:21 A. Yes.</p> <p>....</p> <p>77:11 Q. Did you interact with the 77:12 legal department in connection with their 77:13 counterparty reviews?</p> <p>77:14 A. Yes.</p> <p>77:15 Q. And can you describe that 77:16 interaction?</p>
<b>Bates Moss Tr. at 78:4 – 78:17</b>	<p>78:4 A. Our discussions with, or 78:5 engagement or interaction with predatory 78:6 was really more from the perspective of, 78:7 again, if there were material findings or 78:8 information that could be a data input 78:9 into our overall review of that 78:10 counterparty to determine whether or not 78:11 that counterparty remained a financially 78:12 and operationally sound counterparty,</p>

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	<p>78:13 that at a -- we would speak with John and</p> <p>78:14 Cindy as to sort of are there any issues</p> <p>78:15 we need to be aware of as we consider the</p> <p>78:16 overall financial and creditworthiness of</p> <p>78:17 this institution.</p>
<b>Bates Moss Tr. at 79:8 – 82:18</b>	<p>79:8 Q. Did you become aware that in</p> <p>79:9 conducting their anti-predatory lending</p> <p>79:10 reviews the legal department actually</p> <p>79:11 physically looked at loan files of an</p> <p>79:12 originator?</p> <p>79:14 A. I was aware that that was a</p> <p>79:15 part of their process.</p> <p>79:16 Q. And what did you understand in</p> <p>79:17 that regard?</p> <p>79:18 A. That that was a part of their</p> <p>79:19 process and that they performed such</p> <p>79:20 reviews.</p> <p>79:21 Q. And did you appreciate that</p> <p>79:22 they performed such reviews of</p> <p>79:23 originators who both sold loans directly</p> <p>79:24 to Fannie Mae and who placed loans into</p> <p>79:25 private label securities?</p> <p>80:2 A. Yes.</p> <p>82:8 Q. And would you all, these</p> <p>82:9 groups get together every once in awhile</p> <p>82:10 to talk about the counterparties that you</p> <p>82:11 were reviewing?</p> <p>82:14 A. We would meet for the purposes</p> <p>82:15 of ensuring that we had a, an</p> <p>82:16 enterprise-wide view of the exposures of</p> <p>82:17 a particular counterparty that might be</p> <p>82:18 doing business across Fannie Mae.</p>
<b>Bates Moss Tr. at 107:2 – 108:10</b>	<p>107:2 Q. Was this document something</p> <p>107:3 that was an operative process or</p> <p>107:4 procedure while you were at Fannie Mae?</p> <p>107:5 A. Yes.</p> <p>107:6 Q. Okay. And what did</p> <p>107:7 nontraditional mean here in this document</p> <p>107:8 entitled nontraditional lending group?</p> <p>107:9 A. It meant PLS and other</p>

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	<p>107:10 nontraditional sellers and servicers.  107:11 Q. Did it also mean, refer to as  107:12 subprime loans?</p> <p>107:14 A. Nontraditional included  107:15 subprime.  107:16 Q. Did it also include Alt-A  107:17 loans?</p> <p>107:19 A. It primarily focused on  107:20 subprime.  107:21 Q. Did it also --  107:22 A. PLS.  107:23 Q. Did it also include Alt-A  107:24 loans?</p> <p>108:2 A. I apologize, I'm trying to  108:3 determine at the -- when I arrived at the  108:4 organization.  108:5 Q. At some point during your time  108:6 within Fannie Mae did nontraditional  108:7 lending also refer to Alt-A loans?  108:8 A. It may have included Alt-A,  108:9 but the primary focus was on subprime  108:10 PLS, manufactured housing.</p>
<b>Bates Moss Tr. at 109:14 – 112:19</b>	<p>109:14 Q. Under desk review procedures  109:15 there's a heading below that entitled  109:16 desk review procedures, step 1, second  109:17 sentence states "The functional areas  109:18 that should be reviewed as part of the  109:19 desk review are as follows and do you see  109:20 it goes to list certain items, correct?  109:21 A. Correct.  109:22 Q. And the first item is  109:23 origination, correct?  109:24 A. Correct.  109:25 Q. And under origination it</p> <p>110:2 identifies six areas, A through F, right?  110:3 A. Yes.  110:4 Q. And those include policies,  110:5 procedures, correct? Yes?  110:6 A. Yes.</p>

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110:7 Q. TPOs, third party  
110:8 originations, correct?  
110:9 A. Yes.  
110:10 Q. Appraisal?  
110:11 A. Yes.  
110:12 Q. And underwriting?  
110:13 A. Yes.  
110:14 Q. All of these areas were  
110:15 reviewed as part of a desk review?  
110:16 A. Depending on the specific  
110:17 situation, the desk review may have  
110:18 included some or all of these aspects.  
110:19 Q. Can you recall any  
110:20 counterparty desk review relating to PLS  
110:21 where any of these areas were not  
110:22 reviewed?  
110:23 A. No.  
110:24 Q. If you could turn now, please,  
110:25 to page 546, Bates ending 546 and that's

111:2 entitled "Nontraditional lending group  
111:3 onsite operational review process." Do  
111:4 you see that?  
111:5 A. Yes.  
111:6 Q. And the second paragraph under  
111:7 that states "All issuers and servicers  
111:8 for whom total outstanding investment  
111:9 equals or exceeds \$1 billion must be  
111:10 approved and monitored by the SFMB using  
111:11 established SFMB policies and  
111:12 procedures." Do you see that?  
111:13 A. Yes.  
111:14 Q. Do you recall what established  
111:15 SFMB policies and procedures this is  
111:16 referring to?  
111:17 A. Counterparty credit risk  
111:18 policies and procedures.

111:24 Q. In the next section it's  
111:25 entitled "Operational review procedures,"

112:2 do you see that?  
112:3 A. Yes.

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	<p>112:4 Q. And under step 1 the first</p> <p>112:5 paragraph indicates that the</p> <p>112:6 nontraditional lending group will conduct</p> <p>112:7 an onsite operational review and then</p> <p>112:8 there are five items after that, do you</p> <p>112:9 see that?</p> <p>112:10 A. Yes.</p> <p>112:11 Q. Are those five different</p> <p>112:12 business units within Fannie Mae?</p> <p>112:13 A. Four different business units.</p> <p>112:14 Q. And which are the four</p> <p>112:15 different business units, can you just</p> <p>112:16 identify them?</p> <p>112:17 A. Single family marketing,</p> <p>112:18 legal, credit finance, and nontraditional</p> <p>112:19 and counterparty were consolidated.</p>
<b>Bates Moss Tr. at 113:12 – 114:17</b>	<p>113:12 Q. If you could turn, please, to</p> <p>113:13 the next page, page 547. Do you see that</p> <p>113:14 there is a step 4?</p> <p>113:15 A. Yes.</p> <p>113:16 Q. And do you see it states</p> <p>113:17 "Onsite operational review will consist</p> <p>113:18 of a detailed analysis of the following</p> <p>113:19 areas of operations"? Do you see that?</p> <p>113:20 A. Yes.</p> <p>113:21 Q. And it then lists, among other</p> <p>113:22 things, underwriting, policies, practices</p> <p>113:23 and procedures, origination/acquisition,</p> <p>113:24 policies, practices and procedures, and</p> <p>113:25 aggregator review? Do you see that?</p> <p>114:2 A. Yes.</p> <p>114:3 Q. Under this policy, the onsite</p> <p>114:4 operational review included a detailed</p> <p>114:5 analysis of each of those areas at a</p> <p>114:6 nontraditional lender?</p> <p>114:9 A. Yes, focused on the</p> <p>114:10 operations.</p> <p>114:11 Q. Are you aware of any onsite</p> <p>114:12 review where any of these areas were not</p> <p>114:13 analyzed in detail?</p>

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	<p>114:16 A. I cannot recall a situation 114:17 where they would not be.</p>
<b>Bates Moss Tr. at 117:12 – 121:3</b>	<p>117:12 Q. Okay. If you can turn, 117:13 please, to page 551. Do you see that 117:14 this is entitled "Nontraditional lending 117:15 operational review template" and you see 117:16 that it continues on for pages and pages 117:17 through 564? 117:18 A. Mm-hmm. 117:19 Q. Yes. 117:20 A. Yes, I see that. 117:21 Q. Do you see it lays out 117:22 information that Fannie Mae reviewers 117:23 were to obtain during an onsite 117:24 operational review of a nontraditional 117:25 lender?</p> <p>118:4 A. No. It is information that is 118:5 obtained either from onsite or from the 118:6 responsible parties as input into a final 118:7 report. 118:8 Q. Okay. On page 553 do you see 118:9 that among the areas that Fannie Mae 118:10 obtained information on in connection 118:11 with an onsite operational counterparty 118:12 review was the counterparty's 118:13 origination/underwriting? 118:14 A. That's correct. 118:15 Q. And loan originations? 118:16 A. That's correct. 118:17 Q. And onto the next page, you 118:18 see it also included information 118:19 concerning appraisal quality and 118:20 appraisal processes? 118:21 A. Yes. 118:22 Q. As well as underwriting? 118:23 A. Yes. 118:24 Q. And Fannie Mae would seek 118:25 information concerning these areas during  119:2 an operational review?</p>

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	<p>119:5 A. These are questions that, yes, 119:6 could be -- would be asked.</p> <p>119:7 Q. And just to look at a couple 119:8 of them, on page 553, under 119:9 origination/underwriting review summary, 119:10 the objective is listed as "To obtain 119:11 information with regard to the lenders 119:12 origination processes and to become 119:13 familiar with how the lender originates 119:14 loans." Do you see that?</p> <p>119:15 A. Yes.</p> <p>119:16 Q. Are you aware of any 119:17 counterparty onsite operational review 119:18 where Fannie Mae did not become familiar 119:19 with how a lender originated loans?</p> <p>119:22 A. Analysts that were conducting 119:23 these reviews would interview to 119:24 understand the origination and 119:25 underwriting process for the purpose of</p> <p>120:2 ensuring compliance with Fannie Mae's 120:3 requirements.</p> <p>120:19 Q. So an onsite counterparty 120:20 operational review, the reviewers would 120:21 either be relying on a prior review in 120:22 order to become familiar with how the 120:23 lender originated loans, or would review 120:24 that area themselves anew?</p> <p>121:3 A. That was an option.</p>
<b>Bates Moss Tr. at 147:22 – 154:14</b>	<p>147:22 Q. And on the last page of the 147:23 document, is that your signature on July 147:24 11th, 2006?</p> <p>147:25 A. Yes, it is.</p> <p>....</p> <p>148:2 Q. Indicating that you approved 148:3 this review and the recommendations 148:4 contained in it?</p> <p>148:5 A. Yes.</p> <p>148:6 Q. Would you typically read a 148:7 review before signing it?</p>



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148:8 A. Yes.  
 148:9 Q. Do you happen to recall this  
 148:10 specific review of Fremont in 2006?  
 148:11 A. I do now with the document in  
 148:12 front of me.  
 148:13 Q. It refreshes your recollection  
 148:14 that in fact your group reviewed Fremont  
 148:15 Investment and Loan in May,  
 148:16 approximately, 2006?  
 148:17 A. Yes.  
 148:18 Q. On the second page do you see  
 148:19 the first paragraph indicates that single  
 148:20 family counterparty risk management team  
 148:21 conducted an onsite operational review of  
 148:22 Fremont on May 16th to 17th, 2006 at  
 148:23 Fremont's offices in California, correct?  
 148:24 A. Yes.  
 148:25 Q. And the next sentence states  
  
 149:2 "The review encompassed an in-depth  
 149:3 evaluation of the mortgage origination,  
 149:4 risk management operations, and servicing  
 149:5 operations of Fremont." Do you see that?  
 149:6 A. Yes.  
 149:7 Q. And so Fannie Mae personnel,  
 149:8 Mr. Johnson, Mr. Vignato, were able to  
 149:9 conduct in-depth evaluations of subprime  
 149:10 originators' mortgage origination  
 149:11 processes?  
  
 149:14 Q. Correct?  
 149:15 A. I'm sorry?  
 149:16 Q. Fannie personnel like Mr.  
 149:17 Johnson and Mr. Vignato, were able to  
 149:18 conduct in-depth evaluations of subprime  
 149:19 originators' mortgage origination  
 149:20 processes, correct?  
  
 149:23 A. They conducted an assessment  
 149:24 and review, yes.  
 149:25 Q. And in their terms it was an  
  
 150:2 in-depth evaluation, correct?

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150:3 A. Yes.

150:4 Q. And in the first page when it  
150:5 says nontraditional counterparty  
150:6 operational review, you understood that  
150:7 to include subprime loans and also PLS?

150:10 A. This review was done  
150:11 specifically, as it states in the  
150:12 document, for Fannie Mae's subprime  
150:13 initiative and risk transformation  
150:14 facility, and that Fremont was currently  
150:15 an approved PLS counterparty at the time  
150:16 that this review was done.

150:17 Q. So Fremont's an approved  
150:18 counterparty for PLS transactions at the  
150:19 time this review is done, correct?

150:20 A. Correct.

150:21 Q. And Fannie Mae personnel are  
150:22 now going on site again to Fremont to  
150:23 review its processes and procedures  
150:24 further?

151:3 A. They are going on site to  
151:4 review this, the origination, operational  
151:5 and servicing analysis for the purposes  
151:6 of approving the counterparty as a  
151:7 subprime counterparty.

151:8 Q. Okay.

151:9 A. Under this initiative.

151:10 Q. And when Fannie Mae personnel  
151:11 went on site to conduct this in-depth  
151:12 review of an originator like Fremont,  
151:13 were there any restrictions on what the  
151:14 Fannie Mae reviewers could look at?

151:17 A. As I stated previously, the  
151:18 team conducting the review would review  
151:19 all aspects of the origination,  
151:20 underwriting, servicing process, which  
151:21 would include policies, procedures,  
151:22 processes, you know, loan sampling, etc.

152:9 Q. So in this case, they were

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152:10 looking and did an in-depth evaluation of  
 152:11 mortgage origination and risk management  
 152:12 operations, among other things. Were  
 152:13 there any restrictions on what your  
 152:14 reviewers could look at with respect to  
 152:15 mortgage origination or risk management  
 152:16 operations?

152:19 A. There were no explicit  
 152:20 restrictions, but in this instance, they  
 152:21 were focused on whole loan collateral for  
 152:22 the purposes of becoming an approved  
 152:23 counterparty to sell subprime loans to  
 152:24 Fannie Mae.

152:25 Q. In the second paragraph on the

153:2 page we're on it states, "Based on this  
 153:3 review, it's our recommendation that  
 153:4 Fremont Investment and Loan has  
 153:5 demonstrated appropriate business  
 153:6 practices to mitigate operational and  
 153:7 credit risk of both the origination and  
 153:8 servicing of subprime collateral as well  
 153:9 as financial stability to support the  
 153:10 risk associated with subprime collateral.  
 153:11 Fremont Investment and Loan is currently  
 153:12 an approved Fannie Mae private label  
 153:13 securities counterparty and in good  
 153:14 standing."

153:15 Do you see that?

153:16 A. Yes.

153:17 Q. What business practices did  
 153:18 Fremont use to mitigate operational and  
 153:19 credit risk for the origination of  
 153:20 subprime collateral?

153:23 A. In this instance, the team  
 153:24 felt that the -- that Fremont had strong  
 153:25 risk management, fraud management,

154:2 collateral value review processes in  
 154:3 place to help mitigate some of the items  
 154:4 that they identified that could be

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	<p>154:5 potential risk.</p> <p>154:6 Q. If you could turn, please, to</p> <p>154:7 the page ending Bates 290. Do you see</p> <p>154:8 under the heading collateral performance,</p> <p>154:9 statistics and trending" that the first</p> <p>154:10 paragraph indicates that Fremont</p> <p>154:11 collateral is in securities from its own</p> <p>154:12 shelf and in securities from dealer</p> <p>154:13 shelves, correct?</p> <p>154:14 A. Correct.</p>
<b>Bates Moss Tr. at 154:24 – 156:3</b>	<p>154:24 Q. But the reviewers obviously</p> <p>154:25 understood that Fremont loans were being</p> <p>155:2 placed into private label securities,</p> <p>155:3 correct?</p> <p>155:4 A. That's correct.</p> <p>155:8 If you could turn now, please,</p> <p>155:9 to Bates number, it's 296 to 297. Do you</p> <p>155:10 see there's a heading on 296 called</p> <p>155:11 "underwriting processes"?</p> <p>155:12 A. Yes.</p> <p>155:13 Q. And do you see that the review</p> <p>155:14 team indicated that the underwriting</p> <p>155:15 processes at Fremont were acceptable,</p> <p>155:16 correct?</p> <p>155:17 A. Okay.</p> <p>155:18 Q. Do you see that? Do you see</p> <p>155:19 that the review team indicated that</p> <p>155:20 Fremont's underwriting processes were</p> <p>155:21 acceptable?</p> <p>155:22 A. Yes.</p> <p>155:23 Q. And the way we know that is</p> <p>155:24 because the acceptable box is checked?</p> <p>155:25 A. Is checked.</p> <p>156:2 Q. Correct?</p> <p>156:3 A. Correct.</p>
<b>Bates Moss Tr. at 165:13 – 167:15</b>	<p>165:13 Q. Ms. Bates Moss, we were</p> <p>165:14 looking at the Fremont nontraditional</p> <p>165:15 counterparty operational review. I'd</p> <p>165:16 like to stay in there and ask if you</p>

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165:17 could turn to page 299, Bates stamp 299.

165:18 A. Okay.

165:19 Q. Do you see at the bottom  
165:20 there's a heading called "loan level  
165:21 credit review"?

165:22 A. Yes.

165:23 Q. And do you see that the  
165:24 checked box there indicates that the  
165:25 review team found that the loan level

166:2 credit review was acceptable?

166:3 A. Yes.

166:4 Q. And in the first paragraph it  
166:5 states "The SF CPRM team," that's single  
166:6 family counterparty risk management team?

166:7 A. That's correct.

166:8 Q. "Performed onsite level due  
166:9 diligence, onsite loan level due  
166:10 diligence. The loan sample consisted of  
166:11 the review of 17 loan files," and it  
166:12 describes those, and it then says,  
166:13 "Typically, a risk grade of 4 would not  
166:14 be purchased and kicked from the pool of  
166:15 loans. The risk grade 4 sample  
166:16 represents 12 percent of the population  
166:17 reviewed. Typically, a kickout  
166:18 concentration of 15 percent or less is  
166:19 acceptable. Additional information on  
166:20 each loan reviewed is available as  
166:21 supporting documentation."

166:22 Do you see that?

166:23 A. Yes.

166:24 Q. What's a risk grade 4?

166:25 A. A risk grade 4 according to

167:2 this document would be considered a high  
167:3 risk loan.

167:4 Q. Those are loans that Fannie  
167:5 Mae typically would not purchase and  
167:6 would be kicked from a pool of loans?

167:7 A. According to this, yes.

167:8 Q. And you see that this is  
167:9 reporting that your review team found

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	<p>167:10 that 12 percent of the loans in its  167:11 sample of Fremont loans were a risk grade  167:12 4?  167:13 A. Yes, but it also states that a  167:14 kickout concentration of 15 percent or  167:15 less is acceptable.</p>
<b>Bates Moss Tr. at 168:22 – 170:8</b>	<p>168:22 Q. And you observed that the  168:23 review team reported that typically a  168:24 kickout concentration of 15 percent or  168:25 less is acceptable, do you see that?</p> <p>169:2 A. Yes.  169:3 Q. And that's what you were  169:4 referring to in your prior answer?  169:5 A. That that is, that is a rule  169:6 of thumb that, or a guideline that at the  169:7 time may have been in place, yes.  169:8 Q. Whose rule of thumb was it?  169:9 A. Or guideline.  169:10 Q. Whose rule of thumb or  169:11 guideline was it?  169:12 A. Not rule of thumb, guideline.  169:13 Q. Sorry. Whose guideline was it  169:14 that a kickout concentration of 15  169:15 percent or less was acceptable?  169:16 A. This is handled in credit  169:17 risk.  169:18 Q. So we're talking Fannie Mae's  169:19 guideline was that 15 percent or less of  169:20 kickout loans was acceptable?</p> <p>169:22 A. This does not clarify that  169:23 it's Fannie Mae versus the  169:24 counterparties.</p> <p>170:2 mean when the review team reported that  170:3 typically a kickout concentration of 15  170:4 percent or less is acceptable?  170:5 A. As we stated -- as I stated  170:6 before, this would -- we are doing this  170:7 evaluation relative to Fannie Mae's  170:8 guidelines.</p>

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<b>Bates Moss Tr. at 170:17 – 171:5</b>	<p>170:17 Q. It was acceptable to Fannie 170:18 Mae if up to 15 percent of loans in a 170:19 sample were kicked out as risk grade 4?</p> <p>170:22 A. It was acceptable relative to 170:23 the number of loans that were randomly 170:24 sampled for the purposes of this review. 170:25 Q. Why was a 15 percent kickout</p> <p>171:2 concentration acceptable to Fannie Mae?</p> <p>171:4 A. I cannot speak to why that 171:5 would be acceptable.</p>
<b>Bates Moss Tr. at 172:18 – 177:6</b>	<p>172:18 Q. If you could turn, please, to 172:19 the next page, page 300. Do you see that 172:20 there's a heading called "post-funding 172:21 and quality control process"? 172:22 A. Yes. 172:23 Q. And do you see that this was 172:24 also deemed acceptable to the Fannie 172:25 review team?</p> <p>173:2 A. Yes. 173:3 Q. And to you, since you recall 173:4 you signed the back of this document as 173:5 well, correct? 173:6 A. My approval is for the overall 173:7 process, a review. 173:8 Q. Do you see in the second 173:9 paragraph underneath the post-funding and 173:10 quality control process it states 173:11 "Fremont's quality control department 173:12 conducts a monthly review of a 5 to 10 173:13 percent random sample of the company's 173:14 total loan production. Additionally, a 173:15 targeted 30 percent sample is reviewed 173:16 monthly from each operation center on a 173:17 rotating basis"? 173:18 Do you see that? 173:19 A. Yes. 173:20 Q. And that type of sampling was 173:21 deemed acceptable to the counterparty 173:22 review team?</p>

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173:25 A. If you read the prior

174:2 paragraph, what is acceptable is the  
174:3 overall review of the process and in this  
174:4 -- which includes a number of factors,  
174:5 this being one of them.

174:6 Q. And this factor --

174:7 A. Meaning the quality control  
174:8 department's review process was one of  
174:9 several factors that were considered in  
174:10 the post-funding and quality control  
174:11 process.

174:12 Q. Was there any indication here  
174:13 that your review team found this level or  
174:14 type of sampling to be inadequate in any  
174:15 way?

174:16 A. Again, if that was determined  
174:17 to be the case, and as I'm reading  
174:18 through it, it should have been  
174:19 documented here.

174:20 Q. There's no indication here of  
174:21 anyone at Fannie considering it to be  
174:22 inadequate, correct?

174:23 A. I can only speak to the  
174:24 document in front of me and the people  
174:25 that reviewed it. I cannot speak to

175:2 others outside of this review process.

175:3 Q. Your review of this document  
175:4 though indicates to you that the  
175:5 counterparty review team found that this  
175:6 type or level of sampling was adequate,  
175:7 correct?

175:8 A. This does not speak to the  
175:9 level and type of sampling as being  
175:10 adequate. This speaks to the process,  
175:11 the post-funding and quality control  
175:12 process as being adequate and acceptable.

175:13 Q. Okay. Did you have any reason  
175:14 to believe that the Fannie Mae review  
175:15 team chose loans to sample that it  
175:16 considered to be unrepresentative of



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	<p>175:17 Fremont loans?</p> <p>175:19 A. The process and practice is to 175:20 have a random sampling.</p> <p>175:21 Q. Okay. Are you aware of any 175:22 person or document that indicated that 175:23 Fremont's origination processes differed 175:24 as between loans it sold as whole loans 175:25 and loans it placed into PLS?</p> <p>176:2 A. No, I do not recall that to be 176:3 the case.</p> <p>176:4 Q. If you'd look, please, at page 176:5 298 to 299, do you see at the bottom of 176:6 298 there's a heading, "Appraisal quality 176:7 and review processes"? Do you see that?</p> <p>176:8 A. Yes.</p> <p>176:9 Q. And do you see on 299 it 176:10 indicates that Fremont's appraisal 176:11 quality and review processes were 176:12 acceptable to Fannie Mae? Strike that.</p> <p>176:13 Do you see that on page 298, 176:14 actually, do you see at the bottom it 176:15 indicates that Fremont's appraisal 176:16 quality and review processes were 176:17 acceptable to Fannie Mae?</p> <p>176:18 A. Yes.</p> <p>176:19 Q. And on page 299 in the fifth 176:20 paragraph, in the last sentence do you 176:21 see that it states "Fremont allows an 176:22 appraisal variance of 15 percent for 176:23 loans with an LTV of 80 percent or less 176:24 and 5 percent for loans up to 95 176:25 percent"?</p> <p>177:2 Do you see that?</p> <p>177:3 A. Yes.</p> <p>177:4 Q. What did that mean?</p> <p>177:5 A. In Fremont's process it allows 177:6 for a variance.</p>
<b>Bates Moss Tr. at 182:13 – 182:22</b>	<p>182:13 Q. Sitting here, can you identify 182:14 any originator who had a different 182:15 allowance of appraisal variance than</p>

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	<p>182:16 Fremont?</p> <p>182:17 A. No, I cannot.</p> <p>182:18 Q. Obviously your review team</p> <p>182:19 marked the appraisal quality and review</p> <p>182:20 processes of Fremont acceptable, correct?</p> <p>182:21 A. That's what this document</p> <p>182:22 says, yes</p>
<b>Bates Moss Tr. at 184:4 - 185:4</b>	<p>184:4 Q. With respect to the 15 percent</p> <p>184:5 appraisal variance, is there any</p> <p>184:6 indication here that your reviewers found</p> <p>184:7 it to be a material issue or concern?</p> <p>184:8 A. If it was a material issue or</p> <p>184:9 a concern it would have been reflected in</p> <p>184:10 the overall assessment of the process.</p> <p>184:11 Q. And the overall assessment of</p> <p>184:12 process here was that it was acceptable?</p> <p>184:14 A. Based on this report, it was</p> <p>184:15 marked acceptable.</p> <p>184:16 Q. More broadly, can you recall</p> <p>184:17 anyone at Fannie Mae ever indicating that</p> <p>184:18 an originator having a 15 percent</p> <p>184:19 appraisal variance raised a material</p> <p>184:20 concern or issue?</p> <p>184:22 A. I do not recall that.</p> <p>184:23 Q. Are you aware of anyone ever</p> <p>184:24 indicating that an originator having a 15</p> <p>184:25 percent appraisal variance in its</p> <p>185:2 appraisal processes constituted a</p> <p>185:3 departure from industry standards?</p> <p>185:4 A. No, I do not recall that.</p>
<b>Bates Moss Tr. at 195:6 – 197:17</b>	<p>195:6 Q. And your signature on each of</p> <p>195:7 them is on the same day, July 11, 2006,</p> <p>195:8 right, the Fremont signature and the</p> <p>195:9 First Franklin signature on those two</p> <p>195:10 reviews, correct? You've signed both</p> <p>195:11 reviews on July 11, 2006, correct? Ms.</p> <p>195:12 Bates Moss?</p> <p>195:13 A. Yes.</p> <p>195:14 Q. I'm just asking whether you've</p> <p>195:15 signed this First Franklin review July</p>

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195:16 11th, 2006?  
 195:17 A. Yes. It looks like -- yes, my  
 195:18 signature is there.  
 195:19 Q. If you can turn to the second  
 195:20 page of the review, it's on Bates page  
 195:21 ending 267, do you see that the first  
 195:22 paragraph indicates that the single  
 195:23 family counterparty risk management team  
 195:24 conducted an onsite operational review of  
 195:25 First Franklin on May 24 to 25, 2006 at

196:2 First Franklin's offices in California?  
 196:3 Do you see that?  
 196:4 A. Yes.  
 196:5 Q. And do you see the third  
 196:6 sentence states "The reviews encompassed  
 196:7 an in-depth evaluation of the mortgage  
 196:8 origination, risk management and  
 196:9 servicing operations of First Franklin,"  
 196:10 correct?  
 196:11 A. Yes.  
 196:12 Q. And so this is another  
 196:13 subprime mortgage originator of whom  
 196:14 Fannie conducted an in-depth evaluation  
 196:15 of their mortgage origination operations,  
 196:16 correct?  
 196:17 A. Correct.  
 196:18 Q. And do you see starting at  
 196:19 Bates 274, let's skip over to 274, did  
 196:20 you see that the review by your team  
 196:21 included a review of collateral  
 196:22 performance statistics and trending,  
 196:23 correct?  
 196:24 A. Correct.  
 196:25 Q. And two pages later on 276, do

197:2 you see it also included a loan level  
 197:3 credit review by Clayton, correct?  
 197:4 A. Yes.  
 197:5 Q. And a page later do you see it  
 197:6 also included a review of First  
 197:7 Franklin's production and sourcing,  
 197:8 correct?

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	<p>197:9 A. Yes.</p> <p>197:10 Q. And would that be loan</p> <p>197:11 production?</p> <p>197:12 A. That is correct.</p> <p>197:13 Q. And do you see that as part of</p> <p>197:14 this in-depth evaluation of First</p> <p>197:15 Franklin it also included a review of its</p> <p>197:16 underwriting processes?</p> <p>197:17 A. Yes.</p>
<b>Bates Moss Tr. at 216:15 – 217:9</b>	<p>216:15 Q. And do you see on page 280, a</p> <p>216:16 couple of pages later there's a heading</p> <p>216:17 entitled "Post-funding and quality</p> <p>216:18 control process"?</p> <p>216:19 A. Okay.</p> <p>216:20 Q. And do you see that Fannie Mae</p> <p>216:21 reviewers also found that to be</p> <p>216:22 acceptable?</p> <p>216:23 A. Yes, that's what it says.</p> <p>216:24 Q. In the second paragraph</p> <p>216:25 underneath that heading do you see it</p> <p>217:2 states "FF," First Franklin, "sets a 15</p> <p>217:3 percent annual tolerance level for branch</p> <p>217:4 underwriting errors. Both clerical and</p> <p>217:5 substantive errors uncovered through</p> <p>217:6 sampling procedures are tallied against</p> <p>217:7 the 15 percent benchmark."</p> <p>217:8 Do you see that?</p> <p>217:9 A. Yes.</p>
<b>Bates Moss Tr. at 217:17 – 219:14</b>	<p>217:17 Do you see that Fannie Mae's</p> <p>217:18 review team is reporting that First</p> <p>217:19 Franklin allowed for a 15 percent</p> <p>217:20 underwriting error rate?</p> <p>217:21 A. Yes, that they are reporting</p> <p>217:22 First Franklin's own internal guidelines.</p> <p>217:23 Q. And that includes substantive</p> <p>217:24 underwriting errors, correct?</p> <p>217:25 A. As reported here.</p> <p>218:1 LESIA BATES MOSS</p> <p>218:2 Q. Do you have any reason to</p> <p>218:3 believe that that underwriting error rate</p> <p>218:4 was not standard in the industry?</p>

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	<p>218:7 A. This was a statement made in  218:8 -- by the author of what was communicated  218:9 to him. This was not benchmarked against  218:10 the industry.</p> <p>218:11 Q. Well, as the head of  218:12 counterparty review, can you recall any  218:13 originator that had a lower underwriting  218:14 error rate than 15 percent?</p> <p>218:17 A. Again, I would have to look at  218:18 reviews to see if such information were  218:19 reported.</p> <p>218:20 Q. Sitting here today, can you  218:21 recall any originator that had a lower  218:22 underwriting error rate than 15 percent?</p> <p>218:24 A. Sitting here today I can't  218:25 even remember what I had for breakfast.</p> <p>219:2 No. I can't tell you at this point,  219:3 again, without having something in front  219:4 of me.</p> <p>219:5 Q. Have you seen any documents in  219:6 connection with your preparation for your  219:7 testimony, or can you recall any  219:8 documents indicating that any originator  219:9 of subprime loans had a lower  219:10 underwriting error rate than 15 percent?</p> <p>219:13 A. I don't recall seeing any  219:14 documents that had this language in it.</p>
<b>Bates Moss Tr. at 222:2 – 222:9</b>	<p>222:2 Q. Is there any indication in  222:3 this description of the post-funding and  222:4 quality control process at First Franklin  222:5 that your reviewers found a 15 percent  222:6 rate of underwriting errors to be  222:7 unacceptable?</p> <p>222:8 A. Again, if that were the case,  222:9 it would have been documented here.</p>
<b>Bates Moss Tr. at 222:20 - 223:2</b>	<p>222:20 Are you aware of your  222:21 counterparty review group ever not  222:22 approving an originator for subprime  222:23 transactions because the originator</p>

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	<p>222:24 allowed for a 15 percent underwriting 222:25 error rate?</p> <p>223:2 A. I am not aware of that.</p>
<b>Bates Moss Tr. at 225:24 – 226:20</b>	<p>225:24 Q. Are you aware of any document 225:25 or person indicating that First</p> <p>226:2 Franklin's tolerance of underwriting 226:3 errors differed as between loans sold as 226:4 whole loans and loans placed into PLS?</p> <p>226:7 A. I would have to look at each 226:8 individual review to see whether or not 226:9 that was documented.</p> <p>226:10 Q. Well, my question to you is do 226:11 you recall sitting here any person either 226:12 -- any person or document indicating that 226:13 First Franklin's tolerance of 226:14 underwriting errors at a level of 15 226:15 percent differed as between loans that 226:16 were sold as whole loans and loans that 226:17 were placed into PLS?</p> <p>226:19 A. No, I don't have that 226:20 recollection.</p>
<b>Bates Moss Tr. at 227:7 – 227:21</b>	<p>227:7 Q. If you could turn, please, to 227:8 the second page, Bates 987, do you see 227:9 that under recommendation the review team 227:10 approved of transactions with Saxon?</p> <p>227:11 A. Okay.</p> <p>227:12 Q. If you could turn, please, to 227:13 page 993, Bates stamp 993 there's a 227:14 heading on that page entitled "Loan level 227:15 credit review - Bohan," do you see that?</p> <p>227:16 A. Yes.</p> <p>227:17 Q. And do you see that here it's 227:18 a company called Bohan instead of Clayton 227:19 that's performing the loan level credit 227:20 review?</p> <p>227:21 A. Okay.</p>
<b>Bates Moss Tr. at 228:6 – 229:20</b>	<p>228:6 Do you see that the review 228:7 team filled out the acceptable box?</p> <p>228:8 A. Okay.</p>

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	<p>228:9 Q. With respect to loan level 228:10 credit review? 228:11 A. Okay. 228:12 Q. And the first sentence in this 228:13 paragraph states "Bohan performed loan 228:14 level due diligence on approximately 400 228:15 recently originated loan files"? Do you 228:16 see that? 228:17 A. Yes. 228:18 Q. It continues out of the 400 228:19 loan files, or loans reviewed, only 61, 228:20 or 15.25 percent were classified as an 228:21 event level 3 finding. Do you see that? 228:22 A. Yes. 228:23 Q. Do you have any reason to 228:24 believe that this 15 percent rate of 228:25 event level 3s in sampled loans was</p> <p>229:2 unacceptable to Fannie Mae? 229:3 A. Again, if it were unacceptable 229:4 it should be documented. 229:5 Q. And what's documented here is 229:6 that in fact it was acceptable, correct?</p> <p>229:9 A. That's what that -- that's 229:10 what's documented, yes. 229:11 Q. Are you -- strike that. 229:12 As the head of counterparty 229:13 risk management, were you aware of any 229:14 originator who had a better rate of event 229:15 level 3 loans, meaning better than 15 229:16 percent, less than 15 percent?</p> <p>229:19 A. I don't have a specific 229:20 example, no.</p>
<b>Bates Moss Tr. at 230:25 – 231:12</b>	<p>230:25 Q. Well we know what it is on the 231:2 sample, it was 15 percent?</p> <p>231:4 A. We know that it's 15 percent 231:5 on these particular loans that were 231:6 sampled. 231:7 Q. And my question is did you</p>

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	<p>231:8 have any basis for believing that the</p> <p>231:9 unsampled portion had a better rate?</p> <p>231:12 A. No.</p>
<b>Bates Moss Tr. at 233:15 – 234:10</b>	<p>233:15 Q. Oh, no, I'm sorry, I may have</p> <p>233:16 misspoke. Let me start again. Do you</p> <p>233:17 see that documentation accounted for</p> <p>233:18 about half, 49.18 percent of the event</p> <p>233:19 level 3 findings?</p> <p>233:20 A. Okay.</p> <p>233:21 Q. Do you see that debt ratio</p> <p>233:22 accounted for about 11 percent of the</p> <p>233:23 event level 3 findings, yes?</p> <p>233:24 A. Yes.</p> <p>233:25 Q. And LTV and guidelines</p> <p>234:2 accounted for about 6 percent each for</p> <p>234:3 the event level 3 findings?</p> <p>234:4 A. Yes.</p> <p>234:5 Q. And do you ever recall anyone</p> <p>234:6 indicating within Fannie Mae that these</p> <p>234:7 findings, these bases for findings of</p> <p>234:8 event level 3 were unacceptable to Fannie</p> <p>234:9 Mae?</p> <p>234:10 A. No.</p>
<b>Bates Moss Tr. at 261:22 – 262:6</b>	<p>261:22 Q. So are you aware of any way in</p> <p>261:23 which the way that Clayton performed</p> <p>261:24 services for Fannie Mae differed from the</p> <p>261:25 way Clayton performed services for</p> <p>262:2 issuers of PLS or originators of subprime</p> <p>262:3 loans?</p> <p>262:5 A. I am not aware of those</p> <p>262:6 differences.</p>
<b>Bates Moss Tr. at 288:17 – 288:24</b>	<p>288:17 Q. My question to you is do you</p> <p>288:18 have any recollection of your team ever</p> <p>288:19 finding that the process used by an</p> <p>288:20 issuer of PLS in due diligence to sample</p> <p>288:21 loans was inadequate?</p> <p>288:22 A. I don't recall any specific</p> <p>288:23 example. I'd have to look at the</p> <p>288:24 reviews.</p>



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<b>Bates Moss Tr. at 289:7 – 289:12</b>	<p>289:7 Q. Have you seen any document</p> <p>289:8 indicating that your group ever found</p> <p>289:9 that an issuer of PLS employed inadequate</p> <p>289:10 processes when conducting due diligence</p> <p>289:11 to sample loans?</p> <p>289:12 A. No.</p>
<b>Bates Moss Tr. at 319:21 – 320:5</b>	<p>319:21 Q. And in that context, can you</p> <p>319:22 identify as the head of counterparty risk</p> <p>319:23 management any originator that used a</p> <p>319:24 different origination process when it</p> <p>319:25 generated loans sold as whole loans as</p> <p>320:2 opposed to loans placed in PLS?</p> <p>320:5 A. No.</p>
<b>Bates Moss Tr. at 353:13 – 353:22</b>	<p>353:13 Q. Are you aware of anyone at</p> <p>353:14 Fannie Mae ever indicating to you that</p> <p>353:15 your group should not approve a</p> <p>353:16 counterparty for transactions because the</p> <p>353:17 level of exceptions by which it issued</p> <p>353:18 loans was too high?</p> <p>353:21 A. I never -- I am not aware of</p> <p>353:22 that to be the case.</p>
<b>Bates Moss Tr. at 412:25 – 413:9</b>	<p>412:25 Q. On the second to last page</p> <p>413:2 it's Bates stamped 725. Do you see that</p> <p>413:3 you've approved this review?</p> <p>413:4 A. Yes.</p> <p>413:5 Q. And that's your signature?</p> <p>413:6 A. That is my signature.</p> <p>413:7 Q. And it indicates that Ms.</p> <p>413:8 Johnson also approved it, your boss?</p> <p>413:9 A. That's correct.</p>
<b>Bates Moss Tr. at 414:6 – 414:16</b>	<p>414:6 Q. And in the third paragraph do</p> <p>414:7 you see that it indicates that the</p> <p>414:8 purpose of this review was to evaluate</p> <p>414:9 Countrywide's non-prime wholesale lending</p> <p>414:10 and servicing operations pursuant to the</p> <p>414:11 PLS policy?</p> <p>414:12 A. That's correct.</p> <p>414:13 Q. And so now this is your</p> <p>414:14 group's review of Countrywide in November</p>

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	<p>414:15 of 2005, correct?</p> <p>414:16 A. That's correct.</p>
<b>Bates Moss Tr. at 416:22 – 420:13</b>	<p>416:22 Q. In the paragraph that we were</p> <p>416:23 in, that third paragraph, do you see that</p> <p>416:24 it states "It is our recommendation that</p> <p>416:25 portfolio continues to be able to</p> <p>417:2 purchase asset-backed securities with</p> <p>417:3 underlying collateral originated and/or</p> <p>417:4 serviced by Countrywide"? Do you see</p> <p>417:5 that?</p> <p>417:6 A. Yes.</p> <p>417:7 Q. That was the recommendation of</p> <p>417:8 your group based on their onsite</p> <p>417:9 evaluation of Countrywide?</p> <p>417:10 A. That's correct.</p> <p>417:11 Q. And did you believe that the</p> <p>417:12 people in your group were competent to</p> <p>417:13 perform this evaluation?</p> <p>417:14 A. I believe they were competent</p> <p>417:15 to perform the evaluation on the</p> <p>417:16 counterparty strength and the ability to</p> <p>417:17 continue to do business, yes.</p> <p>417:18 Q. If you could turn, please, to</p> <p>417:19 -- did you have any doubts whatsoever in</p> <p>417:20 the capabilities of the people who were</p> <p>417:21 conducting counterparty reviews in your</p> <p>417:22 group?</p> <p>417:24 A. No.</p> <p>417:25 Q. Did you find them to be</p> <p>418:2 knowledgeable, professional, capable</p> <p>418:3 people?</p> <p>418:5 A. Yes.</p> <p>418:6 Q. And did you give them</p> <p>418:7 favorable performance reviews?</p> <p>418:8 A. Yes, for the most part.</p> <p>418:9 Q. Was there anyone who you</p> <p>418:10 didn't give a favorable performance</p> <p>418:11 review to?</p> <p>418:12 A. I recall one individual, but</p>

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418:13 that individual was not performing these  
418:14 reviews.

418:15 Q. All the people who were  
418:16 performing these reviews you gave  
418:17 favorable performance evaluations to?

418:18 A. That's correct.

418:19 Q. Okay. Including Mr. Johnson  
418:20 and Mr. Vignato?

418:21 A. Correct.

418:22 Q. If you could turn, please, to  
418:23 Bates stamp ending 716, it's page 8 of 17  
418:24 of the document. Do you see there's a  
418:25 heading there in the middle of the page

419:2 called "Underwriting"?

419:3 A. Yes.

419:4 Q. And on the next page in that  
419:5 section do you see that in the second  
419:6 paragraph on the next page it states  
419:7 "Underwriters have the ability to grant  
419:8 guideline exceptions, e.g. FICO, 50  
419:9 percent DTI, if three compensating  
419:10 factors exist. Examples of compensating  
419:11 factors include length of time borrower's  
419:12 on the job or disposable income sources.  
419:13 There's a 20 percent exception rate and  
419:14 there are 18 levels of authority to sign  
419:15 off on exceptions."

419:16 Do you see that?

419:17 A. Yes.

419:18 Q. What did you understand an  
419:19 exception rate to be when reported here  
419:20 by your review team?

419:21 A. Again, these section writeups  
419:22 are descriptions of the counterparty's  
419:23 process. So my understanding of what is  
419:24 presented here is that Greg Johnson was  
419:25 documenting the results of the interview

420:2 with the counterparty, and this is the  
420:3 counterparty's explanation of the  
420:4 counterparty's guidelines and process.

420:5 Q. And what was your

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	<p>420:6 understanding of what a 20 percent  420:7 exception rate was?  420:8 A. As I stated yesterday, the  420:9 exception rate, pursuant to their  420:10 guidelines, is these are the loans that  420:11 they would, looking at those factors, may  420:12 kickout or approve for other compensating  420:13 factors.</p>
<b>Bates Moss Tr. at 425:9 – 426:2</b>	<p>425:9 Q. So is there any indication  425:10 here that your review team had any  425:11 objection to the fact that Countrywide  425:12 reported to it that it issued 20 percent  425:13 of the loans that it originated as  425:14 exceptions to Countrywide's underwriting  425:15 guidelines?</p> <p>425:17 A. I do not see any such language  425:18 in this document as presented that would  425:19 suggest that. If it were the case, it  425:20 would have been documented.</p> <p>425:21 Q. And in fact, under the summary  425:22 up above you do see that the  425:23 recommendation of the relationship is to  425:24 continue the relationship with  425:25 Countrywide?</p> <p>426:2 A. That's correct.</p>
<b>Bates Moss Tr. at 433:10 – 434:3</b>	<p>433:10 Q. Okay. Looking at page 717  433:11 under the heading "Post-closing and  433:12 quality control," do you see that?  433:13 A. Yes.</p> <p>433:14 Q. If you can go on to the next  433:15 page, do you see that the first paragraph  433:16 states, "The QC staff also reviews those  433:17 loans where there's a 15 percent variance  433:18 between the BPO and appraisal." Do you  433:19 know what a BPO is?  433:20 A. A broker -- a broker price  433:21 opinion.</p> <p>433:22 Q. And so the reviewers here are  433:23 reporting that Countrywide's QC staff  433:24 reviews loans if there's a 15 percent  433:25 variance between the broker price opinion</p>

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	<p>434:2 and appraisal?</p> <p>434:3 A. Yes.</p>
<b>Feigles Tr. at 142:2 – 142:13</b>	<p>142:2 Q. So I take it your group was</p> <p>142:3 responsible, then, for reviews of loan</p> <p>142:4 originators whose product went into PLS in</p> <p>142:5 which Freddie invested?</p> <p>142:6 A. Yes, to the best of my knowledge.</p> <p>142:7 Q. And reviews of loan aggregators</p> <p>142:8 whose product -- who securitized those loans</p> <p>142:9 and sold PLS to Freddie Mac?</p> <p>142:10 A. That's right.</p> <p>142:11 Q. And then also diligence for T deals,</p> <p>142:12 correct?</p> <p>142:13 A. Yes.</p>
<b>Feigles Tr. at 154:2 – 154:16</b>	<p>154:2 Q. Were there different types of</p> <p>154:3 reviews you would conduct?</p> <p>154:5 BY MR. BENNETT:</p> <p>154:6 Q. Different scopes?</p> <p>154:8 THE WITNESS: Yeah. We had</p> <p>154:9 originators, servicer, and aggregator reviews.</p> <p>154:10 BY MR. BENNETT:</p> <p>154:11 Q. And of the originators, were they</p> <p>154:12 different scopes you would do with different</p> <p>154:13 originators, or did they all get essentially</p> <p>154:14 the same review?</p> <p>154:15 A. To the best of my knowledge, they</p> <p>154:16 all got generally the same review.</p>
<b>Feigles Tr. at 155:4 – 155:20</b>	<p>155:4 Q. So from the subject of the review,</p> <p>155:5 you would ask for performance data?</p> <p>155:6 A. Correct.</p> <p>155:7 Q. And what kind of performance data?</p> <p>155:8 A. We may get loans that they've</p> <p>155:9 originated depending on the -- we may get</p> <p>155:10 performance of the loans they originated. We</p> <p>155:11 may get their servicing data. It's an</p> <p>155:12 aggregator, pools that states, you know, what</p> <p>155:13 they were rated, that they've securitized. It</p> <p>155:14 would be what they provided us.</p> <p>155:15 Q. So with respect to performance data</p> <p>155:16 from an originator on how loans performed,</p>

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	155:17	would that be -- include things like the
	155:18	default rate?
	155:20	THE WITNESS: It's possible.
<b>Feigles Tr. at 156:6 – 21</b>	156:6	Q. Would you sometimes get diligence
	156:7	results on previously processed pools?
	156:9	THE WITNESS: Possibly. I don't
	156:10	recall.
	156:11	BY MR. BENNETT:
	156:12	Q. And then, I take it, you would look
	156:13	at the -- the prior reviews of whoever --
	156:14	whatever organization you were going to review?
	156:16	THE WITNESS: That's right.
	156:17	BY MR. BENNETT:
	156:18	Q. And you have those in a file
	156:19	someplace where you could go access them?
	156:20	A. We have the AMO reviews that we
	156:21	could go access.
<b>Feigles Tr. at 170:23 – 172:2</b>	170:23	Q. Okay. So let's go back to the first
	170:24	page, which is 617. The first paragraph is
	170:25	titled "Background," and it reads: "The
	171:2	primary function of the alternative market
	171:3	operations unit, AMO, is conduct operational
	171:4	reviews. These reviews are used to help
	171:5	Freddie Mac's internal business units make
	171:6	decisions about which business partners to
	171:7	pursue and where to set position limits."
	171:8	Is that an accurate statement of
	171:9	what the primary function of the AMO unit
	171:10	was --
	171:12	BY MR. BENNETT:
	171:13	Q. -- during your time?
	171:15	THE WITNESS: It probably was in
	171:16	2005. Specifically, I didn't have any insight
	171:17	into position limits. I didn't -- I don't know
	171:18	how they were determined or -- or set.
	171:19	BY MR. BENNETT:
	171:20	Q. Okay. And you don't know how or

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	171:21	whether they considered your reviews in setting
	171:22	position limits?
	171:24	THE WITNESS: My understanding was
	171:25	they did certainly use our reviews in their
	172:2	analysis. I don't understand how.
<b>Feigles Tr. at 172:20 – 173:15</b>	172:20	Q. Was it a prerequisite to doing
	172:21	business with Freddie Mac as a sub -- subprime
	172:22	or Alt-A loan originator that you submit to an
	172:23	alternative markets operations review?
	172:25	THE WITNESS: So, generally
	173:2	speaking, that's my understanding.
	173:3	BY MR. BENNETT:
	173:4	Q. Do you know of any cases where a
	173:5	subprime or Alt-A originator was allowed to do
	173:6	business with Freddie Mac, who -- which had not
	173:7	submitted itself to an AMO review?
	173:9	THE WITNESS: So I generally recall
	173:10	a conversation with either Mike Aneiro or Dave
	173:11	Hackney where they indicated that they could
	173:12	purchase some di minimus amount of -- of
	173:13	security backed by loans that we were -- that
	173:14	we had not done an AMO review without an AMO
	173:15	review.
<b>Feigles Tr. at 174:4 – 174:11</b>	174:4	Q. Do you recall whether they actually
	174:5	did go ahead and purchase a PLS that was
	174:6	backed, at least, in part by an unreviewed
	174:7	originator?
	174:9	THE WITNESS: I don't know what
<b>Feigles Tr. at 174:18 – 175:6</b>	174:10	securities they bought or what was comprised in
	174:11	the securities they bought.
	174:18	Q. And did they give you a reason why
	174:19	it was okay for them to make those kinds of
	174:20	purchases?
	174:22	THE WITNESS: I'm trying to recall
	174:23	the context and -- and how it came up. To the
	174:24	best of my recollection, we had a counterparty
	174:25	that was up for review, I don't remember who it

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	<p>175:2 was, and I think we asked them should we go see  175:3 this guy or this company. My recollection is  175:4 they said, no, we occasionally see a handful of  175:5 their loans in -- in a security, but not enough  175:6 to warrant sending you out there.</p>
<b>Feigles Tr. at 175:18 – 176:15</b>	<p>175:18 Q. And the first sentence reads: "The  175:19 base origination scope consists of a 50-loan  175:20 file review plus an interview with management."  175:21 Do you see that?  175:22 A. I see that.  175:23 Q. Was 50 the base number of loans that  175:24 were to be reviewed?</p> <p>176:2 THE WITNESS: That's what it says  176:3 here.  176:4 BY MR. BENNETT:  176:5 Q. And did you, on occasion, review  176:6 more than 50 loans?  176:7 A. My recollection is that occasionally  176:8 we might.  176:9 Q. Under what circumstances might you  176:10 review more than 50 loans?  176:11 A. I'm not sure what circumstances, but  176:12 my recollection is that I think there were some  176:13 instances where we did look at more than 50.  176:14 Q. Would that be based on your  176:15 assessment of potential risks?</p>
<b>Feigles Tr. at 177:22 – 178:4</b>	<p>177:22 Q. This paragraph goes on to read:  177:23 "Files are selected for the review by the AMO  177:24 lead on a random basis from a tape of the  177:25 counterparty's most recent months' production;"  178:1 RONALD FEIGLES  178:2 is that accurate?</p> <p>178:4 THE WITNESS: I believe so.</p>
<b>Feigles Tr. at 178:23 – 180:13</b>	<p>178:23 Q. Did you then do a -- or not then,  178:24 but did you also do management interviews?  178:25 A. Yes.</p> <p>179:2 Q. And the management interviews  179:3 touched on credit, appraisal, control and fair  179:4 lending and corporate governance?</p>



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	<p>179:6 THE WITNESS: They did in 2005.  179:7 BY MR. BENNETT:  179:8 Q. Did that change?  179:9 A. Certainly the categories changed in  179:10 2006 at some point.  179:11 Q. And what categories were added, to  179:12 your recollection?  179:13 A. I think fair lending changed to  179:14 anti-predatory lending. I don't know if we  179:15 changed underwriting or credit to underwriting,  179:16 corporate governance. I don't think -- we  179:17 renamed that to be something corporate  179:18 structure, something like that.  179:19 Q. Did it change the substance of what  179:20 you were doing?</p> <p>179:22 THE WITNESS: I think to some  179:23 respect we did.  179:24 BY MR. BENNETT:  179:25 Q. And why was that change made?</p> <p>180:3 THE WITNESS: I don't recall  180:4 specifically why we made those changes.  180:5 BY MR. BENNETT:  180:6 Q. Do you recall generally why you made  180:7 those changes?</p> <p>180:9 THE WITNESS: We were trying to  180:10 refine our -- our practice and, you know, we  180:11 were operating under trying to improve our  180:12 processes and our practices. That's why we  180:13 made those changes.</p>
<b>Feigles Tr. at 181:6 – 181:16</b>	<p>181:6 Q. I think you might have misspoke.  181:7 You said you received a list of 50 loans from  181:8 the seller?  181:9 A. I'm sorry. We received a list of  181:10 the previous months' -- that's right. Previous  181:11 months' originations and we selected 50 off of  181:12 that list.  181:13 Q. But today you don't recall how you  181:14 made that selection?  181:15 A. My -- best of my recollection it was  181:16 just a random selection.</p>

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<b>Feigles Tr. at 182:5 – 182:23</b>	182:5	So you would -- you would select 50
	182:6	loans and review those loans to check, among
	182:7	other things, compliance with guidelines,
	182:8	correct?
	182:9	A. Right.
	182:10	Q. And these were loans that were
	182:11	originated by originators who were feeding some
	182:12	production into the collateral pools underlying
	182:13	PLS in which Freddie was investing, correct?
	182:15	THE WITNESS: Most likely, yes.
	182:16	BY MR. BENNETT:
	182:17	Q. Was there any procedure in place to
	182:18	prevent you from reviewing loans from these
<b>Feigles Tr. at 186:9 – 187:13</b>	182:19	originators where those loans might later end
	182:20	up in a collateral pool underlying a Freddie
	182:21	Mac security?
	182:23	THE WITNESS: No.
	186:9	Q. If you flip ahead to 1630, there's a
	186:10	subheading in the middle of the page,
	186:11	"Operational Review Components."
	186:12	A. I see that.
	186:13	Q. And the second sentence reads: "The
	186:14	purpose of the operational review is to ensure
	186:15	a comprehensive understanding of the customers'
	186:16	processes and to assess alignment with Freddie
	186:17	Mac."
	186:18	Is that an accurate description of
	186:19	the purpose of the reviews during your tenure?
	186:21	THE WITNESS: I would say in my
	186:22	tenure, alignment with Freddie Mac is very
	186:23	broad and I don't know that I could make that
	186:24	statement, but that's what we were assessing.
	186:25	BY MR. BENNETT:
	187:2	Q. Okay. So setting aside the second
	187:3	clause, then, fair statement that the purpose
	187:4	during your tenure was to ensure comprehensive
	187:5	understanding of the customers' processes?
	187:7	THE WITNESS: As much as we could

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	<p>187:8 understand in a one-day interview.</p> <p>187:9 BY MR. BENNETT:</p> <p>187:10 Q. And also based on preparation?</p> <p>187:11 A. Our file review and our preparation.</p> <p>187:12 Q. And your file review, correct?</p> <p>187:13 A. Correct.</p>
<b>Feigles Tr. at 187:17 – 187:22</b>	<p>187:17 Q. So I take it you at least sought to</p> <p>187:18 gain an understanding -- a comprehensive</p> <p>187:19 understanding of their processes?</p> <p>187:21 THE WITNESS: We certainly wanted to</p> <p>187:22 gain as much of an understanding as we could.</p>
<b>Feigles Tr. at 188:20 – 191:12</b>	<p>188:20 Q. Well, let me just jump through some</p> <p>188:21 specific examples. I just want to focus on</p> <p>188:22 what you were looking at during your reviews.</p> <p>188:23 If you like at the top of 1631 under "Credit</p> <p>188:24 Quality," there are several bullets. The first</p> <p>188:25 one is "Credit Philosophy."</p> <p>189:2 A. Uh-huh.</p> <p>189:3 Q. Is that something you looked at?</p> <p>189:5 THE WITNESS: Yes.</p> <p>189:6 BY MR. BENNETT:</p> <p>189:7 Q. What is -- what does credit</p> <p>189:8 philosophy mean?</p> <p>189:9 A. So we would ask the management, you</p> <p>189:10 know -- you know, ostensibly exactly what's</p> <p>189:11 written here. What's your credit philosophy,</p> <p>189:12 like what -- what market are you going after?</p> <p>189:13 What's -- you know, are -- are you a very</p> <p>189:14 conservative lender? Do you have maybe more</p> <p>189:15 liberal guidelines, but very tight controls?</p> <p>189:16 What's your philosophy. How -- how do you</p> <p>189:17 approach this business?</p> <p>189:18 Q. The second one is "Credit Guidelines</p> <p>189:19 Policies and Procedures." That's something you</p> <p>189:20 looked at, I take it?</p> <p>189:22 THE WITNESS: Yes.</p> <p>189:23 BY MR. BENNETT:</p> <p>189:24 Q. And you reviewed loan files to make</p> <p>189:25 sure that they complied with the guidelines,</p>

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	190:2	policies and procedures, correct?
	190:4	THE WITNESS: We reviewed the files
	190:5	to get a sense of what they did.
	190:6	BY MR. BENNETT:
	190:7	Q. And whether they complied with the
	190:8	guidelines, correct?
	190:10	THE WITNESS: So I would say that
	190:11	certainly, you know, we established that we
	190:12	looked at 50 loans. I don't know that that's a
	190:13	sufficient sample of anybody's work to draw
	190:14	stringent conclusions about whether they
	190:15	adhered or didn't adhere to guidelines. A
	190:16	goal, certainly, to understand if they adhered
	190:17	to credit guidelines.
	190:18	BY MR. BENNETT:
	190:19	Q. And at least with respect to the 50
	190:20	loans you looked at, you were looking to see
	190:21	whether they adhered to guidelines, correct?
	190:23	THE WITNESS: Yes.
	190:24	BY MR. BENNETT:
	190:25	Q. The next one is "Credit Exceptions."
	191:2	What does that mean?
	191:3	A. So do they allow exceptions? Could
	191:4	be that.
	191:5	Q. Exceptions to their guidelines
	191:6	regarding credit, is that what they're
	191:7	referring to?
	191:8	A. Yes.
	191:9	Q. And did -- in your experience, did
	191:10	originators on occasion grant exceptions to
	191:11	their credit guidelines?
	191:12	A. Yes.
<b>Feigles Tr. at 191:19 – 191:22</b>	191:19	Q. Some originators granted many
	191:20	exceptions, some granted fewer, correct?
	191:22	THE WITNESS: Correct.
<b>Feigles Tr. at 194:3 – 195:2</b>	194:3	Q. And what would be the utility to you
	194:4	of receiving a delinquency report?

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	<p>194:6 THE WITNESS: Well, depending on 194:7 what we received and -- and the format, it 194:8 could show loan quality trends. 194:9 BY MR. BENNETT: 194:10 Q. And would that be useful to you in 194:11 understanding the quality of the underwriting 194:12 practices?</p> <p>194:14 THE WITNESS: To the extent that 194:15 they existed at that time, yes. 194:16 BY MR. BENNETT: 194:17 Q. To the extent that the delinquency 194:18 report existed at that time? 194:19 A. Well, to the extent that, you know, 194:20 had their policies and procedures changed over 194:21 time. 194:22 Q. And I suppose that's something you 194:23 would ask them about in their interviews, 194:24 correct?</p> <p>195:2 THE WITNESS: Correct</p>	
<b>Feigles Tr. at 203:14 – 204:8</b>	<p>203:14 Q. Do you remember something called a 203:15 counterparty forum? 203:16 A. No, not off the top of my head, I 203:17 don't remember counterparty forum. 203:18 Q. The next sentence reads: "One 203:19 significant change will be the shifting of our 203:20 report focus from subjectively evaluating the 203:21 originator's credit guidelines to better gauge 203:22 how well they execute against their guidelines 203:23 and the adequacy of their processes to mitigate 203:24 areas of risk." 203:25 Do you see that?</p> <p>204:2 A. I see that. 204:3 Q. First of all, do you recall 204:4 receiving feedback from anyone in 2006 204:5 regarding focusing on originator's compliance 204:6 with their underwriting guidelines?</p> <p>204:8 THE WITNESS: No.</p>	
<b>Feigles Tr. at</b>	205:5 Q. Sure. Was something you had	

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**205:5 – 207:15**

205:6 observed during your time at Freddie Mac the  
205:7 need to focus your reviews more on  
205:8 underwriter's compliance with their  
205:9 underwriting guidelines?

205:11 THE WITNESS: I don't recall if  
205:12 there was anything we observed that had us  
205:13 change the focus of our reviews.

205:14 BY MR. BENNETT:

205:15 Q. Do you know why you changed the  
205:16 focus of your reviews?

205:17 A. Well, while I don't recall  
205:18 specifically having conversations around the  
205:19 focus of our reviews, it's my belief that we  
205:20 did have conversations with capital markets and  
205:21 customer credit management and maybe other  
205:22 constituencies inside of Freddie Mac about the  
205:23 scope of our reviews and how it can provide  
205:24 more value.

205:25 Q. And was there something about noting

206:2 compliance with underwriting guidelines that  
206:3 would add more value to your reports to your  
206:4 understanding?

206:5 A. Since I don't remember the specifics  
206:6 of the conversations, I can't really say.

206:7 Q. Looking back on it now, and based on  
206:8 your years of experience, what do you think the  
206:9 value add would be from focusing on compliance  
206:10 with underwriting guidelines?

206:12 THE WITNESS: Well, certainly you  
206:13 want to know if they adhere to the guidelines  
206:14 for the credit parameters that are established.  
206:15 I mean, that is something you would want to  
206:16 understand.

206:17 BY MR. BENNETT:

206:18 Q. You, being Freddie Mac, would want  
206:19 to understand that?

206:21 THE WITNESS: Yes, us being Freddie  
206:22 Mac.

206:23 BY MR. BENNETT:

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	206:24	Q. And why would Freddie Mac want to
	206:25	understand that?
	207:3	THE WITNESS: Well, to the extent
	207:4	that we are going to have some type of either
	207:5	relationship or investment in something that is
	207:6	backed by their originations, we want to be
	207:7	informed.
	207:8	BY MR. BENNETT:
	207:9	Q. And it was one of the goals of the
	207:10	AMO process to collect that information to
	207:11	allow Freddie Mac to be informed about that,
	207:12	correct?
	207:14	THE WITNESS: It was one avenue of
	207:15	providing information internally.
<b>Feigles Tr. at 213:12 – 214:9</b>	213:12	Q. What was the purpose of an AMO job
	213:13	checklist in this time period?
	213:14	A. It was to provide consistency.
	213:15	Q. Provide consistency to the AMO
	213:16	review process?
	213:17	A. Yes.
	213:18	Q. If you look in here, there are a
	213:19	couple of major headings. The first one is
	213:20	"planning the on-site review," followed by
	213:21	"contact the counterparty," followed by "after
	213:22	the review has been confirmed, sampling in good
	213:23	size, tracking requested items upon arrival and
	213:24	while on site, review testing checklist and
	213:25	upon returning from the site visit."
	214:2	Was this document meant to be a
	214:3	guide for the AMO review teams as they
	214:4	completed every phase of the AMO review
	214:5	process?
	214:7	THE WITNESS: Again, while I don't
	214:8	recall specifically utilizing this, it appears
	214:9	so, yes.
<b>Feigles Tr. at 219:16 – 221:13</b>	219:16	Q. Sure. The resources listed here
	219:17	under: "Planning the on-site review," those
	219:18	were to be drawn upon in planning your on-site
	219:19	AMO reviews?

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219:21 THE WITNESS: Yes.  
 219:22 BY MR. BENNETT:  
 219:23 Q. If you flip to the page ending in  
 219:24 Bates No. 1197, it is Page 3 of the document.  
 219:25 There is a section titled: "After the review  
  
 220:2 has been confirmed."  
 220:3 And then there are several boxes.  
 220:4 If you go down, there is a box that begins with  
 220:5 the word "perform." "Perform LexisNexis rating  
 220:6 agencies and/or Internet company website  
 220:7 searches."  
 220:8 Do you see that?  
 220:9 A. I see that.  
 220:10 Q. Do you recall searching LexisNexis  
 220:11 for information about AOM review  
 220:12 counterparties?  
 220:13 A. Vaguely.  
 220:14 Q. And you were also guided by this  
 220:15 form to check rating agency websites for  
 220:16 information about counterparties as well,  
 220:17 correct?  
  
 220:19 THE WITNESS: That's correct.  
 220:20 BY MR. BENNETT:  
 220:21 Q. Did you also conduct Internet  
 220:22 searches regarding counterparties?  
 220:23 A. It appears we did.  
 220:24 Q. Did you also look at regulatory and  
 220:25 SEC websites regarding counterparties?  
  
 221:2 A. Again, it would appear so.  
 221:3 Q. And did you look at -- inside B&C  
 221:4 Lending and Mortgage Servicing News and other  
 221:5 industry publications?  
  
 221:7 THE WITNESS: I believe we did.  
 221:8 BY MR. BENNETT:  
 221:9 Q. Now if you go to the bottom of the  
 221:10 page, there is a cell regarding prereview  
 221:11 conference calls.  
 221:12 Do you see that?



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	221:13	A. I see that.
<b>Feigles Tr. at 252:25 – 254:9</b>	252:25	Q. Let's flip to the Bates number
	253:2	ending in 194. It's Page 10, where we were a
	253:3	moment ago.
	253:4	Are you there?
	253:5	A. I am.
	253:6	Q. In the purpose section, this is
	253:7	going to look -- I think we read similar
	253:8	language a while ago.
	253:9	It reads: "The primary function of
	253:10	the AMO unit is to conduct operational reviews.
	253:11	These reviews are used to help Freddie Mac's
	253:12	internal business units make decisions about
	253:13	which business partners to pursue and where to
	253:14	set position limits."
	253:15	Do you see that?
	253:16	A. I see that.
	253:17	Q. Does this refresh your recollection
	253:18	at all about what you meant by setting position
	253:19	limits?
	253:20	A. Again, we provided a tool that -- or
	253:21	a work product that other parties used
	253:22	internally at Freddie Mac, and I believe one of
	253:23	those parties set position limits.
	253:24	Q. And position limits would be limits
	253:25	on how much exposure Freddie Mac could take in
	254:2	terms of investing in the loans originated by a
	254:3	certain originator, for example?
	254:5	THE WITNESS: For example, yes.
	254:6	BY MR. BENNETT:
	254:7	Q. Can you think of other examples of
	254:8	position limits that this would affect?
	254:9	A. Not off the top of my head.

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<b>Gussman Tr. at 113:19-115:20</b>	<p>113:19 Q. Do you remember if shortly 113:20 after you arrived you changed or modified 113:21 the collateral reports that the 113:22 surveillance team was putting together? 113:23 A. I made a large number of 113:24 changes, so, but I can't point to a 113:25 specific one and when.</p> <p>114:2 Q. Do you recall changes that you 114:3 would have made early on when you were at 114:4 Fannie Mae? 114:5 A. What I recall early on at 114:6 Fannie Mae was working more on this loan 114:7 level model with CJ than the surveillance 114:8 reports. I'm sure we were making changes 114:9 to everything, but that's -- I remember 114:10 my focus being on the analytics side. 114:11 Q. So is there anything else you 114:12 can recall other than the loan level 114:13 model with CJ and the surveillance work 114:14 you talked about that you were doing in 114:15 the time period in, say, the first six 114:16 months after you joined Fannie Mae?</p> <p>114:18 A. Our main push at that time was 114:19 building this loan level model that CJ 114:20 was responsible for. I'm sure I was 114:21 presented with a large variety of 114:22 possibilities as a new boss and people 114:23 were looking to get their project 114:24 sponsored essentially, but my main push 114:25 when I got there was to work with CJ on</p> <p>115:2 this loan level model. 115:3 Q. And that was something she was 115:4 already working on before you joined? 115:5 A. It was -- there were some 115:6 forms of the models that existed some 115:7 place else before I got there. 115:8 Q. Do you recall in this time 115:9 period being involved in the pre-purchase 115:10 review of specific securitizations?</p>

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	<p>115:11 A. I recall that we instituted a</p> <p>115:12 pre-purchase review process and we did</p> <p>115:13 apply it to some deals. I couldn't tell</p> <p>115:14 you the exact dates of when those</p> <p>115:15 happened, but that, that process took</p> <p>115:16 place.</p> <p>115:17 Q. You applied the pre-purchase</p> <p>115:18 review process to some RMBS deals that</p> <p>115:19 Fannie Mae actually ended up purchasing?</p> <p>115:20 A. That's correct.</p>
<b>Gonzalez-Rey Tr. at 30:8-25</b>	<p>30:8 Q Let's turn to the second of the two analytic</p> <p>30:9 systems that traders used when they were making</p> <p>30:10 decisions to purchase PLS. TAC, what was --</p> <p>30:11 (Interruption by teleconference system.)</p> <p>30:12 Q How did they use TAC?</p> <p>30:13 A So that's an analytics they can access.</p> <p>30:14 It's internal analytics, and I guess by how to use --</p> <p>30:15 can you be more specific how they would use that?</p> <p>30:16 Q Why did they use it? What did it tell them?</p> <p>30:17 A It would also produce some evaluation risk</p> <p>30:18 metrics for the securities.</p> <p>30:19 Q Valuation risk metrics?</p> <p>30:20 A Uh-hmm.</p> <p>30:21 Q And what were those?</p> <p>30:22 A Some of the ones I mentioned before, OAS. I</p> <p>30:23 believe, also, OAD.</p> <p>30:24 Q And what is OAD?</p> <p>30:25 A Option-adjusted duration.</p>
<b>Gonzalez-Rey Tr. at 31:10-24</b>	<p>31:10 Q When traders were deciding what price to pay</p> <p>31:11 for PLS, what tool, model, system, analytics did they</p> <p>31:12 use?</p> <p>31:14 A They used the systems that I would describe,</p> <p>31:15 and, also, at a certain period of time, they would --</p> <p>31:16 they would -- do you mean systems?</p> <p>31:17 Q System, model, tool, analytics.</p> <p>31:18 A Okay. So at a certain point in time, they</p> <p>31:19 started using a recommendation from a group of</p> <p>31:20 analysts in the Capital Markets Strategies group.</p> <p>31:21 Q Prior to the time they took recommendations</p> <p>31:22 from CMS, what did they use to price bonds?</p> <p>31:23 A They would use the tools I mentioned, TAC</p> <p>31:24 and Intex GUI.</p>

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**Kain Tr. at  
188:21 -- 190:16**

188:21 Q. If you look down in the table below  
188:22 there is -- there are a series of processes  
188:23 listed, and the second one down reads: "Deal  
188:24 analysis."  
188:25 Do you see that?

189:2 A. Uh-huh. Yes, I do.  
189:3 Q. It reads: "PM," which is portfolio  
189:4 managers, "must conduct a transaction viability  
189:5 analysis to evaluate each trading opportunity."  
189:6 What does that mean?  
189:7 A. It -- I am looking at it now and  
189:8 interpreting that. They have to decide whether  
189:9 the transaction makes sense, is the way I read  
189:10 that, and I think the next line is probably  
189:11 more instructive which says the "PM calculates  
189:12 the return on equity and evaluates other  
189:13 important factors," and so generally the  
189:14 attempt was or the mindset here is it had to  
189:15 hit an ROE threshold, and that is what, you  
189:16 know, that was kind of the -- if it hit the ROE  
189:17 threshold then it was a viable investment,  
189:18 assuming you looked at other factors and there  
189:19 was no other factor why you didn't want to buy  
189:20 it.  
189:21 Q. Do you recall what the ROE threshold  
189:22 was during that time period?  
189:23 A. It varied. It was at one point --  
189:24 most of the time it was 15. There were times  
189:25 when we temporarily raised it and I think it

190:2 got lowered at some point, but 15 is the number  
190:3 that comes to mind more often than not.  
190:4 Q. Do you remember it being nine for a  
190:5 period of time?  
190:6 A. I think there were exceptions where  
190:7 it was lowered, but nine seems low.  
190:8 Q. Is the ROE threshold different than  
190:9 the hurdle?  
190:10 A. I don't believe so.  
190:11 Q. And where it mentions in the second  
190:12 sentence: "Other important factors," is that a  
190:13 reference to the housing goals?

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	<p>190:15 THE WITNESS: I don't know. That is</p> <p>190:16 very possible.</p>
Norris Tr. at 64:3 -- 65:13	<p>64:3 Q. At the time you joined the</p> <p>64:4 mortgage portfolio in mid to late 2005,</p> <p>64:5 what was the process Fannie Mae went</p> <p>64:6 through when it purchased a private label</p> <p>64:7 security?</p> <p>64:9 A. A dealer, generically</p> <p>64:10 speaking, there would be an offering from</p> <p>64:11 a dealer. There was an initial list of</p> <p>64:12 collateral that was shown to us in an</p> <p>64:13 offering memorandum and other numerous</p> <p>64:14 documentations, like a prospectus</p> <p>64:15 supplement, an initial prospectus</p> <p>64:16 supplement, sales documents, offering</p> <p>64:17 memorandum, etc., that we would look at</p> <p>64:18 for statistics that we wanted to see,</p> <p>64:19 meaning credit documentation.</p> <p>64:20 Then if we were interested in</p> <p>64:21 the deal based on price and credit, then</p> <p>64:22 a data tape would be sent to Fannie Mae's</p> <p>64:23 data warehouse, which was on the other</p> <p>64:24 side of the business, and that would be</p> <p>64:25 scrubbed of nonpublic information,</p> <p>65:2 because there was a firewall between us</p> <p>65:3 and single family. And nonpublic</p> <p>65:4 information would be scrubbed from, from</p> <p>65:5 this tape and a CDI file would be sent to</p> <p>65:6 us containing summarized data.</p> <p>65:7 We would then take that data,</p> <p>65:8 analyze it for structure, credit, price,</p> <p>65:9 and determine if we wanted to participate</p> <p>65:10 in the deal and what collateral we wanted</p> <p>65:11 to keep or not keep.</p> <p>65:12 I forgot one important point.</p> <p>65:13 It was always scored for housing goals</p>
Norris Tr. at 114:2 -- 115:15	<p>114:2 Q. If you look at the next page</p> <p>114:3 in the procedure manual that's part of</p> <p>114:4 Exhibit 608, section 4.1 describes</p> <p>114:5 process steps.</p>

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	<p>114:6 A. Mm-hmm.</p> <p>114:7 Q. The first one, 4.1.1, "A</p> <p>114:8 nonagency mortgage trader is contacted by</p> <p>114:9 a dealer for the purposes of facilitating</p> <p>114:10 a private label MBS transaction."</p> <p>114:11 Did you, Mr. Salahuddin and</p> <p>114:12 Ms. Dyson divide among you different</p> <p>114:13 dealers? In other words, did you, did</p> <p>114:14 you have certain dealers that you dealt</p> <p>114:15 with, Mr. Salahuddin had certain other</p> <p>114:16 dealers that he dealt with?</p> <p>114:17 A. No.</p> <p>114:18 Q. So when a dealer called to</p> <p>114:19 offer a PLS, how did you determine whose</p> <p>114:20 responsibility that deal would be?</p> <p>114:21 A. At that time it was simply</p> <p>114:22 who, who had the work at the time, I</p> <p>114:23 guess. So there was always overlap</p> <p>114:24 between one deal versus another. So who</p> <p>114:25 had the bandwidth to do a deal. Not --</p> <p>115:2 or to analyze the deal or start the deal.</p> <p>115:3 Q. And was that a decision you</p> <p>115:4 made?</p> <p>115:5 A. It was.</p> <p>115:6 Q. The next process step says</p> <p>115:7 "The nonagency mortgage trader confers</p> <p>115:8 with the director of the nonagency</p> <p>115:9 mortgage desk to determine interest in</p> <p>115:10 executing the trade."</p> <p>115:11 Do you see that?</p> <p>115:12 A. Mm-hmm. Yes.</p> <p>115:13 Q. Who's the director of the</p> <p>115:14 nonagency mortgage desk?</p> <p>115:15 A. That would be me.</p>
<b>Salahuddin Tr. at 520:20 -- 522:3</b>	<p>520:20 Q. I believe you testified</p> <p>520:21 earlier that you analyzed deals to</p> <p>520:22 determine whether they made sense for</p> <p>520:23 Fannie Mae from an economic perspective</p> <p>520:24 and from a credit perspective, have I got</p> <p>520:25 that right?</p> <p>521:2 A. I did do analysis related to</p>

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	<p>521:3 both of those things, yes.</p> <p>521:4 Q. What other analysis did you do</p> <p>521:5 in the course of determining whether to</p> <p>521:6 buy a particular residential</p> <p>521:7 mortgage-backed security?</p> <p>521:9 A. I can recall there being</p> <p>521:10 instances where I would check to ensure</p> <p>521:11 that the collateral that was being</p> <p>521:12 provided in the -- and the information</p> <p>521:13 about the deal that was being provided</p> <p>521:14 complied to our list of stipulations.</p> <p>521:15 In addition to economic and</p> <p>521:16 credit analysis, we would also provide</p> <p>521:17 analysis -- be recipient of analysis</p> <p>521:18 around the goals -- how certain loans, or</p> <p>521:19 how the loans of the population</p> <p>521:20 contributed or did not contribute to</p> <p>521:21 housing goals, and so some analysis would</p> <p>521:22 have been done around that information as</p> <p>521:23 well to determine the degree to which any</p> <p>521:24 particular loan is accretive or</p> <p>521:25 detrimental to housing goals.</p> <p>522:2 And I believe that's, that's</p> <p>522:3 all I can remember right now.</p>
<p><b>Kenneweg</b>  <b>30(b)(6) Tr. at</b>  <b>40:23 -- 42:12</b></p>	<p>40:23 Q. Yes. Please identify, if you</p> <p>40:24 would, all departments or business units</p> <p>40:25 within Freddie Mac who were involved in the</p> <p>41:2 review or evaluation of PLS counterparties.</p> <p>41:4 A. What type of --</p> <p>41:7 A. What type of review and</p> <p>41:8 evaluation?</p> <p>41:9 Q. Any review that involves</p> <p>41:10 considering information concerning those</p> <p>41:11 counterparties, forming an opinion, rendering</p> <p>41:12 an evaluation, or issuing an approval.</p> <p>41:15 BY MR. SECHLER:</p> <p>41:16 Q. So it could include operational</p>

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	<p>41:17 reviews, financial reviews. Reviews of any 41:18 kind.</p> <p>41:21 A. I would say counterparty credit 41:22 risk, and the alternative markets operations 41:23 group.</p> <p>41:24 Q. Was there also a group known as 41:25 external operations risk management, or EORM?</p> <p>42:2 A. Yes.</p> <p>42:3 Q. Were they also involved in the 42:4 review of counterparties for PLS?</p> <p>42:5 A. No.</p> <p>42:6 Q. What was the nature of their 42:7 responsibilities?</p> <p>42:8 A. They reviewed counterparties -- 42:9 their scope was the prime business that was 42:10 delivered to Freddie Mac for guaranty -- for 42:11 the guaranty side. So seller/servicers, 42:12 originations that would be delivered into APC.</p>
<b>Kenneweg 30(b)(6) Tr. at 42:23 -- 43:22</b>	<p>Q. We haven't been that 42:24 productive. And could you identify the 42:25 document that I have just handed you?</p> <p>43:2 A. It looks like an e-mail. The 43:3 subject is MABS Policies/Procedures.</p> <p>43:4 Q. Is this an e-mail from you?</p> <p>43:5 A. It is.</p> <p>43:6 Q. That you sent on or about 43:7 December 10, 2009?</p> <p>43:8 A. Yes.</p> <p>43:9 Q. And what are you attaching to 43:10 this e-mail?</p> <p>43:11 A. It looks like a procedure for 43:12 PLS counterparty. Let's see what else. And a 43:13 policy and procedure, um, also related to PLS, 43:14 owned by another area.</p> <p>43:15 Q. Okay. So the document we have 43:16 attached is MABS Counterparty Procedure Number 43:17 123. Right?</p> <p>43:18 A. Yes.</p> <p>43:19 Q. And is that what is attached to</p>



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	<p>43:20 this e-mail, the MABS Counterparty Procedure  43:21 123?  43:22 A. It is.</p>
<b>Kenneweg Tr. 30(b)(6) at 88:17 -- 89:10</b>	<p>88:17 Q. Sure. These AMO written  88:18 reviews, they were used to determine whether  88:19 or not to approve a PLS counterparty?</p> <p>88:22 A. That wasn't the sole use, but  88:23 it was a consideration.  88:24 Q. Well, that was a use?  88:25 A. Right. Right.</p> <p>89:2 Q. They were also used to develop  89:3 a metric score for PLS counterparties. Right?  89:4 A. Correct.  89:5 Q. And they were used in  89:6 connection with the ongoing monitoring of PLS  89:7 counterparties. Correct?</p> <p>89:10 A. Yes.</p>
<b>Kenneweg 30(b)(6) Tr. at 88:17 -- 89:10</b>	<p>88:17 Q. Sure. These AMO written  88:18 reviews, they were used to determine whether  88:19 or not to approve a PLS counterparty?</p> <p>88:22 A. That wasn't the sole use, but  88:23 it was a consideration.  88:24 Q. Well, that was a use?  88:25 A. Right. Right.</p> <p>89:2 Q. They were also used to develop  89:3 a metric score for PLS counterparties. Right?  89:4 A. Correct.  89:5 Q. And they were used in  89:6 connection with the ongoing monitoring of PLS  89:7 counterparties. Correct?</p> <p>89:10 A. Yes.</p>
<b>Kenneweg 30(b)(6) Tr. at 242:17 -- 244:25</b>	<p>242:17 Q. Did Freddie Mac have any  242:18 policies or procedures that prevented it from  242:19 buying PLS whose loans came from originators  242:20 who scored 4 in the credit and appraisal  242:21 areas?</p>

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242:24 A. There were lots of things that  
242:25 were assessed in a PLS purchase, including

243:2 credit enhancement, guarantees, so, um, I  
243:3 think it would be -- no, our policies did not  
243:4 focus specifically on that one criteria.  
243:5 Since there's -- there could be mitigating  
243:6 circumstances.

243:7 Q. Ultimately your policies with  
243:8 respect to purchasing PLS depended on  
243:9 application of that grid we looked at in PM&P  
243:10 101, right?

243:13 A. That's right.

243:14 Q. And that depended on the M  
243:15 score assigned to a particular counterparty  
243:16 originator, right?

243:19 A. Yes. M score, right, was  
243:20 referenced in the table.

243:21 Q. And we saw on that table that  
243:22 it didn't really matter what the M score was  
243:23 for an originator if the aggregator was M-1 to  
243:24 M-5, right?

244:2 form. Scope and foundation.

244:3 A. I think that's too broad of a  
244:4 statement, to say it just doesn't matter what  
244:5 the M score was. People could still consider  
244:6 it. But as far as what the policy prescribed,  
244:7 as far as being, um, preapproved, yes, as long  
244:8 as you had an aggregator that was rated at a  
244:9 certain rating, that's right, the deal could  
244:10 be approved.

244:11 Q. Regardless of what the M rating  
244:12 was for the originator?

244:15 A. That's right.

244:16 Q. And regardless of what rating  
244:17 AMO assigned in the credit and appraisal  
244:18 sections of its AMO scorecard?

244:21 BY MR. SECHLER:

PLS Pre-Purchase Process	
	<p>244:23 A. Right. In consideration of</p> <p>244:24 other variables on the deal also. That's</p> <p>244:25 right.</p>
<b>Anciro Tr. at 239:17 -- 240:10</b>	<p>239:17 Q. So is it fair to say that</p> <p>239:18 before a PLS purchase occurred, the</p> <p>239:19 following steps took place: A dealer</p> <p>239:20 provides strats for the Freddie loans and</p> <p>239:21 for the aggregate loans to a trader; is</p> <p>239:22 that right?</p> <p>239:23 A. Yes.</p> <p>239:24 Q. And Freddie Mac runs the deal</p> <p>239:25 through Mortgage Pricer; is that right?</p> <p>240:1 A. Correct.</p> <p>240:2 Q. And runs the ROE calculator;</p> <p>240:3 is that right?</p> <p>240:4 A. Correct.</p> <p>240:5 Q. And conducts a housing goals</p> <p>240:6 analysis, right?</p> <p>240:7 A. Correct.</p> <p>240:8 Q. Determines which prepayment</p> <p>240:9 models to use?</p> <p>240:10 A. I think that would be a step.</p>

**Factors GSE PLS Traders Considered When Making the Decision to Purchase PLS****Norris Tr. at 67:3  
-- 25**

67:3 Q. If I understood you correctly,  
67:4 you said if you were interested in the  
67:5 deal based on price and credit, you would  
67:6 ask for a loan tape?

67:7 A. No, we would already have a  
67:8 scrubbed loan tape. We would -- that's  
67:9 what a CDI file is. CDI file contains  
67:10 structure and the characteristics of the  
67:11 pool.

67:12 Q. So the CDI file would come at  
67:13 the time you got the strats?

67:14 A. Yeah, if we agreed that we  
67:15 wanted to look at the deal, that's  
67:16 correct.

67:17 Q. So pausing there, what factors  
67:18 did you consider to decide whether you  
67:19 wanted to look at a deal?

67:20 A. I would say the intersection  
67:21 of housing goals, price, and collateral,  
67:22 each one being fairly important. By the  
67:23 way, when I say price, I mean credit  
67:24 enhancement as well as price of the  
67:25 security.

**Norris Tr. at 71:7  
-- 74:6**

71:7 Q. Did Fannie Mae have written  
71:8 guidelines that you looked to when you  
71:9 were assessing these various factors to  
71:10 determine whether a deal did or didn't  
71:11 meet your investment requirements?

71:12 A. Can you explain that a little  
71:13 further? Do you mean Fannie Mae as the  
71:14 entity, myself as Fannie Mae, like what,  
71:15 what part of --

71:16 Q. Was there any written policy  
71:17 or procedure that set forth, for example,  
71:18 required metrics?

71:19 A. There were some metrics --

71:22 THE WITNESS: Sorry, I keep  
71:23 doing that.

71:24 A. There were some metrics that  
71:25 were provided by us as the private label

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72:2 group as you've been describing us. I  
72:3 don't recall any other metrics. They  
72:4 were more guidelines other than, you  
72:5 know, certain things had to be done. In  
72:6 other words, the reps and warrants  
72:7 provided to us, anti-predatory lending  
72:8 standards, HOEPA, I'm trying to think the  
72:9 other things that were out there, rep and  
72:10 warrants, the housing goals validity, and  
72:11 that they did the due diligence sampling.  
72:12 Q. When you say that they did the  
72:13 due diligence sampling, you're talking  
72:14 about the dealer?  
72:15 A. Correct.  
72:16 Q. Did due diligence sampling for  
72:17 what purpose?  
  
72:19 A. To make sure the loans were  
72:20 what they said they were.  
72:21 Q. And was there a required  
72:22 percentage of loans that dealers had to  
72:23 sample?  
72:24 A. I don't recall.  
72:25 Q. And all of these factors you  
  
73:2 just mentioned, where were they written  
73:3 down?  
73:4 A. I don't recall.  
73:5 Q. Are these things that you  
73:6 provided to dealers in writing?  
  
73:8 A. I don't recall. I know that  
73:9 our lawyers were in contact with possibly  
73:10 the Street's lawyers and that there were  
73:11 things in place before I had gotten there  
73:12 regarding reps and warrants and validity  
73:13 of were these loans charter compliant.  
73:14 That's about the extent of my knowledge  
73:15 on that.  
73:16 Q. Was it part of your  
73:17 responsibility to make sure that all of  
73:18 these reps and warrants were complied  
73:19 with before executing a trade?

**Factors GSE PLS Traders Considered When Making the Decision to Purchase PLS**

	<p>73:20 A. I'm trying to think that there  73:21 were some things that we would look at in  73:22 the documentation, but I don't think we  73:23 were looking at, we weren't reviewing all  73:24 the, all the reps and warrants. I  73:25 believe there was another group that was</p> <p>74:2 looking at those as well.  74:3 Q. Do you know what group that  74:4 was?  74:5 A. I thought it was one of the  74:6 legal teams.</p>
<p><b>Norris Tr. at  115:16 -- 117:5</b></p>	<p>115:16 Q. So what would you and a trader  115:17 discuss in determining Fannie Mae's  115:18 interest in executing a trade?</p> <p>115:20 A. I don't recall specifics, but  115:21 it would be, generally speaking, what is  115:22 the price, what is the collateral and  115:23 what is the housing goals.  115:24 Q. And that's all something that  115:25 you would be able to determine at this</p> <p>116:2 stage of the process?  116:3 A. Not necessarily, no. Most  116:4 times, no.  116:5 Q. 4.1.3 says "The dealer sorts  116:6 conforming collateral based on Fannie  116:7 Mae's stipulations."  116:8 What were Fannie Mae's  116:9 stipulations?  116:10 A. I don't recall exactly, but I  116:11 know that we had a loosely put together  116:12 sheet that had our starting guidelines,  116:13 and I don't mean Fannie Mae guidelines,  116:14 but the private label desk guidelines,  116:15 meaning some of the things that we talked  116:16 loosely about before are -- and again,  116:17 this depends exactly on what time frame  116:18 we're talking about, because they were  116:19 constantly changing, but -- not  116:20 constantly changing, but changing. As an  116:21 example, we may have at that time limited</p>

<b>Factors GSE PLS Traders Considered When Making the Decision to Purchase PLS</b>	
	<p>116:22 the number of second liens that were  116:23 allowed in a pool. We may have limited  116:24 the amount of LTV.  116:25 But it was always that one of</p> <p>117:2 the stipulations were reps and warrants  117:3 to Fannie guidelines, housing goals, due  117:4 diligence, and -- I can't remember the  117:5 last part.</p>
<b>Syron Tr. at 273:21 -- 274:12</b>	<p>273:21 Q. It's the paragraph that begins  273:22 with "Syron offered a spirited defense."  273:23 A. I don't know if I agreed -- I  273:24 don't know if I agreed to increase the  273:25 purchasing of risky mortgages early in  274:1  274:2 this decade to fulfill the company's  274:3 mandate. I think what we tried to do was  274:4 that we tried to find, as in with the AAA  274:5 rated mortgage-backed securities, ways of  274:6 meeting the housing goals to take that in  274:7 a way that was safe and sound.  274:8 Q. I'd like to ask you to look at  274:9 Exhibit 34620, it's the transcript from  274:10 the Financial Crisis Inquiry Commission.  274:11 I think it's the top one on your stack  274:12 here.</p>
<b>D. Cook Tr. at 278:18 -- 280:16</b>	<p>278:18 Q Have you had a chance to take a look at  278:19 what's been marked as Exhibit 614?  278:20 A Yes.  278:21 Q Does this reflect that in pursuit of  278:22 increased purchases for subprime goals, Mr. Norris  278:23 listed ten items that Capital Markets should consider  278:24 that would alter their ordinary practices with respect  278:25 to PLS or other transactions?</p> <p>279:3 A As I read this, this only relates to housing  279:4 goals. It doesn't talk about the fact that to also  279:5 increase -- actually, I don't see anything -- does it  279:6 talk about housing goals here?  279:7 Q "Below is a list of possible exceptions that  279:8 we will need to increase our purchases for subprime  279:9 goals."  279:10 Do you understand that to be referring to</p>

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	<p>279:11 housing goals?</p> <p>279:12 A Not necessarily.</p> <p>279:13 Q What do you think "subprime goals" refers</p> <p>279:14 to?</p> <p>279:15 A This could have been a desire to invest in</p> <p>279:16 more subprime collateral and, hence, get a larger</p> <p>279:17 return. It could have been related to housing goals</p> <p>279:18 also, but I don't read it that way.</p> <p>279:19 Q Had you heard that there was a goal to</p> <p>279:20 invest in more subprime?</p> <p>279:22 A I had heard, and I believe it might have</p> <p>279:23 been in 2006, that Fannie Mae -- I hadn't heard this</p> <p>279:24 goal specifically.</p> <p>279:25 Q You had not heard that there was a goal to</p> <p>280:2 purchase more subprime?</p> <p>280:3 A I hadn't heard this goal specifically as</p> <p>280:4 it's referring to. I had heard, in this era of 2006,</p> <p>280:5 and I'm not sure of the exact dates, there were goals</p> <p>280:6 in Fannie Mae to increase subprime business, but</p> <p>280:7 not -- not necessarily in PLS. I think that was in</p> <p>280:8 our whole loan purchases.</p> <p>280:9 Q The individuals on this e-mail are on the</p> <p>280:10 Capital Markets PLS side, correct?</p> <p>280:11 A Paul Norris was the director. Steve Shen</p> <p>280:12 was his boss. And Ramon de Castro was his boss --</p> <p>280:13 manager. And they all were related -- or worked in</p> <p>280:14 PLS. Andrew Bon Salle was not directly related to</p> <p>280:15 PLS. He was the SVP of Capital Markets Mortgage</p> <p>280:16 Assets but not directly over PLS.</p>
<b>D. Cook Tr. at 250:14 -- 16</b>	<p>250:14 A The charter act has language in it that</p> <p>250:15 requires -- I believe it requires Fannie Mae to meet</p> <p>250:16 certain housing goals as set by HUD.</p>
<b>D. Cook Tr. at 252:16 -- 254:22</b>	<p>252:16 Q What did it mean to engage in activities</p> <p>252:17 that involved a reasonable economic return that may be</p> <p>252:18 less than the return earned on other activities as you</p> <p>252:19 understood it at Fannie Mae in the period 2005 to</p> <p>252:20 2007?</p> <p>252:22 A As I understood this at Fannie Mae, Fannie</p> <p>252:23 Mae was required to meet certain goals, to serve, as</p> <p>252:24 it says, low- and moderate-income families and</p>



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252:25 underserved areas, and those goals were set by HUD,

253:2 and Fannie Mae was tracked in terms of its ability or,  
253:3 rather, its meeting of those goals.

253:4 Q Is it fair to say that those goals that you  
253:5 described were referred to at Fannie Mae sometimes as  
253:6 its mission?

253:8 A I wouldn't interpret the mission as -- as  
253:9 related -- rather, the mission was broader, to me,  
253:10 than just these particular housing goals, and that's  
253:11 the way it was communicated to me. To me, the mission  
253:12 involved all of the items, 1, 2, 3, 4, and 5.

253:13 Q So Fannie Mae's mission involved the five  
253:14 items that were set forth under the National Mortgage  
253:15 Association's purposes act by Congress in Exhibit 602,  
253:16 topic 9, tab 1; is that correct?

253:18 A That's how I understood it.

253:19 Q Was that how you understood Fannie Mae, the  
253:20 institution, to regard its mission?

253:22 A That's how I understood Fannie Mae, the  
253:23 institution, to understand its mission.

253:24 Q Did you hear that set of goals described as  
253:25 the mission when you were at Fannie Mae, and as you

254:2 are at Fannie Mae, from 2005 to 2007?

254:4 A I heard language very similar to this  
254:5 language that described our goals.

254:6 Q Did you hear it called the mission?

254:8 A People at Fannie Mae talked about the  
254:9 mission.

254:10 Q What did you understand them to mean?

254:12 A I understood the mission at Fannie Mae to be  
254:13 to promote stability in the secondary market, to  
254:14 promote liquidity, and to meet our housing goals,  
254:15 which were tracking how well we served underserved  
254:16 areas and low- to moderate-income families.

254:17 Fannie Mae also had a responsibility to its

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	<p>254:18 shareholders to provide a return.</p> <p>254:19 Q Did you understand that Fannie Mae regarded</p> <p>254:20 the mission, as you've described it, as important?</p> <p>254:22 A Yes.</p>
<b>Aneiro Tr. at 239:17 -- 240:10</b>	<p>239:17 Q. So is it fair to say that</p> <p>239:18 before a PLS purchase occurred, the</p> <p>239:19 following steps took place: A dealer</p> <p>239:20 provides strats for the Freddie loans and</p> <p>239:21 for the aggregate loans to a trader; is</p> <p>239:22 that right?</p> <p>239:23 A. Yes.</p> <p>239:24 Q. And Freddie Mac runs the deal</p> <p>239:25 through Mortgage Pricer; is that right?</p> <p>240:1 A. Correct.</p> <p>240:2 Q. And runs the ROE calculator;</p> <p>240:3 is that right?</p> <p>240:4 A. Correct.</p> <p>240:5 Q. And conducts a housing goals</p> <p>240:6 analysis, right?</p> <p>240:7 A. Correct.</p> <p>240:8 Q. Determines which prepayment</p> <p>240:9 models to use?</p> <p>240:10 A. I think that would be a step.</p>

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<b>D. Cook Tr. at 68:19 – 69:5</b>	<p>68:19 Q What does it mean to size and price credit 68:20 risk in this context?</p> <p>68:21 A So sizing the deal was understanding the 68:22 risk associated with the deal and whether the 68:23 structure supported the senior tranches with -- that 68:24 we purchased. And then pricing was, you know, if -- 68:25 if the credit of the deal was a AAA tranche, then they</p> <p>69:2 could infer a price that they would -- they would want 69:3 to receive, in other words, a yield that they would 69:4 want to receive. So if we paid par for a bond, we 69:5 would want to get a return above some benchmark.</p>
<b>D. Cook Tr. at 69:23 – 71:8</b>	<p>69:23 Q Do you know what factors went into that 69:24 determination?</p> <p>69:25 A Which -- what determination?</p> <p>70:2 Q The determination of price.</p> <p>70:3 A I know one of the main determinants was 70:4 whether or not the bond was AAA. If -- if the bond 70:5 was AAA and the traders felt comfortable, through 70:6 their analysis, with the structure and the credit, 70:7 then they had the authority -- I mean, the traders had 70:8 the authority to purchase.</p> <p>70:9 Q Did they have the authority to determine 70:10 what price at -- at what price they would purchase a 70:11 bond?</p> <p>70:12 A The traders?</p> <p>70:13 Q Yes.</p> <p>70:14 A Did have that authority.</p> <p>70:15 Q And were there written procedures that 70:16 guided how they exercised that authority?</p> <p>70:17 A I don't know.</p> <p>70:18 Q Do you know what procedures they followed to 70:19 guide that authority?</p> <p>70:20 A Trade -- what procedure traders followed to 70:21 exercise their pricing authority?</p> <p>70:22 Q Yes.</p> <p>70:23 A I don't believe they had procedures to 70:24 exercise pricing authority.</p> <p>70:25 Q How did they come to a determination of</p>

PLS Traders' Review of Offering Documents	
	<p>71:2 whether a price asked for a PLS was appropriate?</p> <p>71:3 A They used their judgment. They looked in</p> <p>71:4 the market to see what prevailing prices were. They</p> <p>71:5 analyzed the offering materials to ensure they were</p> <p>71:6 comfortable with the deal. And through that analysis</p> <p>71:7 of the deal, they were able to determine what they</p> <p>71:8 felt the right price would be.</p>
<b>D. Cook Tr. at 77:8 – 78:14</b>	<p>77:8 Q The change that gave Capital Markets</p> <p>77:9 Strategy a role in the process is reflected in the</p> <p>77:10 policies and the procedures, correct?</p> <p>77:11 A Yes.</p> <p>77:12 Q Were you a participant in the changes to</p> <p>77:13 those policies and procedures?</p> <p>77:14 A Yes.</p> <p>77:15 Q As a participant in that process, do you</p> <p>77:16 know what drove the changes?</p> <p>77:18 A I have some understanding of what drove the</p> <p>77:19 change.</p> <p>77:20 Q What's your understanding?</p> <p>77:22 A One consideration was the traders, in</p> <p>77:23 working with the dealers, there just was a set amount</p> <p>77:24 of time that they had to accomplish the analysis</p> <p>77:25 before we could commit to deals, and so there was some</p> <p>78:2 reluctance to create a lengthy due diligence process</p> <p>78:3 because we didn't want to necessarily slow down or --</p> <p>78:4 slow down the process. So at first -- but there was</p> <p>78:5 also a desire to provide additional resources or</p> <p>78:6 additional insight from a dedicated risk team.</p> <p>78:7 So in weighing those -- those two competing</p> <p>78:8 priorities of trying to get the deal done but also</p> <p>78:9 making sure that there was independent risk view,</p> <p>78:10 first the risk team started doing presettlement</p> <p>78:11 reviews. Then they started doing precommitment</p> <p>78:12 reviews once they were able to implement a process</p> <p>78:13 that was fast enough to accommodate the traders and</p> <p>78:14 the, sort of, the deal flow.</p>
<b>Aneiro Tr. at 239:17 – 241:17</b>	<p>239:17 Q So is it fair to say that</p> <p>239:18 before a PLS purchase occurred, the</p> <p>239:19 following steps took place: A dealer</p>

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239:20 provides strats for the Freddie loans and  
 239:21 for the aggregate loans to a trader; is  
 239:22 that right?  
 239:23 A. Yes.  
 239:24 Q. And Freddie Mac runs the deal  
 239:25 through Mortgage Pricer; is that right?  
 240:1 A. Correct.  
 240:2 Q. And runs the ROE calculator;  
 240:3 is that right?  
 240:4 A. Correct.  
 240:5 Q. And conducts a housing goals  
 240:6 analysis, right?  
 240:7 A. Correct.  
 240:8 Q. Determines which prepayment  
 240:9 models to use?  
 240:10 A. I think that would be a step.  
  
 240:12 A. Before using Mortgage Pricer.  
 240:13 Q. Conducts a credit analysis?  
 240:14 A. Correct.  
 240:15 Q. There has to be a credit  
 240:16 approval for the deal; is that correct?  
 240:17 A. Correct.  
 240:18 Q. And then the trade is  
 240:19 finalized on a trade ticket? Well I  
 240:20 guess first the trade is communicated to  
 240:21 the dealer; is that right?  
 240:22 A. Correct.  
 240:23 Q. And then the trade is  
 240:24 finalized on a trade ticket?  
 240:25 A. Correct.  
 241:1 Q. And then Freddie Mac receives  
 241:2 a prospectus supplement; is that right?  
 241:3 A. I don't recall the timing of  
 241:4 the supplement.  
 241:5 Q. Okay. Was anything else  
 241:6 required before a PLS trade could occur?  
  
 241:8 A. I don't recall.  
 241:9 Q. You don't recall whether  
 241:10 anything else was required?  
 241:11 A. Correct.  
 241:12 Q. Okay. Can you sitting here

PLS Traders' Review of Offering Documents	
	<p>241:13 today, can you think of anything else  241:14 that was required before a PLS deal could  241:15 occur?</p> <p>241:17 A. I can't.</p>
<b>Aneiro Tr. at 359:9 – 363:5</b>	<p>359:9 Q. All right. Now, during 2005  359:10 to 2007 did Freddie Mac typically receive  359:11 a prospectus supplement for PLS that it  359:12 purchased?</p> <p>359:13 A. I believe so.</p> <p>359:14 Q. When?</p> <p>359:15 A. I don't recall.</p> <p>359:16 Q. Was it after the trade  359:17 commitment date?</p> <p>359:18 A. I don't recall.</p> <p>359:19 Q. What was your practice with  359:20 respect to prospectus supplements for  359:21 deals where you were the portfolio  359:22 manager in charge?</p> <p>359:24 A. I don't recall. I don't  359:25 recall a policy for it.</p> <p>360:1 Q. Sorry, I wasn't asking a  360:2 policy. Your practice for deals where  360:3 you were the trader, what did you do with  360:4 prospectus supplements?</p> <p>360:5 A. I don't --</p> <p>360:7 A. I don't recall.</p> <p>360:8 Q. Did you generally read them?</p> <p>360:9 A. The whole prospectus  360:10 supplement?</p> <p>360:11 Q. Start there, the whole  360:12 prospectus supplement?</p> <p>360:13 A. No.</p> <p>360:14 Q. Did you generally read any  360:15 part of a prospectus supplement?</p> <p>360:16 A. I would look -- I would scan  360:17 through various supplements.</p> <p>360:18 Q. Various supplements meaning  360:19 you wouldn't scan through every  360:20 supplement you received?</p> <p>360:21 A. Correct.</p>

**PLS Traders' Review of Offering Documents**

360:22 Q. But some of them you would  
360:23 scan through?  
360:24 A. Correct.  
360:25 Q. For some deals?  
361:1 A. Correct.  
361:2 Q. When you scanned through a  
361:3 prospectus supplement, which parts did  
361:4 you look at?  
361:5 A. I don't recall.  
361:6 Q. Can you recall any parts that  
361:7 you looked at?  
361:8 A. Not really, no.  
361:9 Q. Do you have any understanding  
361:10 of what others in the nonagency group  
361:11 did, what their practices were with  
361:12 respect to prospectus supplements?  
361:13 A. I do not.

361:15 Q. Did you expect that the people  
361:16 working under you were reading the  
361:17 prospectus supplement for every deal they  
361:18 traded?  
361:19 A. No.  
361:20 Q. Did you expect that the people  
361:21 who worked under you were reading any  
361:22 part of the prospectus supplement for  
361:23 every deal they traded?  
361:24 A. No.  
361:25 Q. Do you have an understanding  
362:1 of the practice with respect to  
362:2 prospectus supplements of those who  
362:3 provided the credit approval?  
362:4 A. I'm sorry, one more time.  
362:5 Q. Do you have any understanding  
362:6 of the practice with respect to  
362:7 prospectus supplements of those who  
362:8 provided credit approval for PLS deals?  
362:10 A. I don't.  
362:11 Q. You don't know if they read  
362:12 the prospectus supplements or not?  
362:13 A. I don't believe they did.  
362:14 Q. Did anyone at Freddie Mac  
362:15 other than a portfolio manager, somebody

PLS Traders' Review of Offering Documents	
	<p>362:16 on the nonagency desk or somebody  362:17 providing credit approval for a deal read  362:18 a prospectus supplement?  ....  362:21 Q. Did anyone at Freddie Mac --  362:22 are you aware of anyone at Freddie Mac,  362:23 other than the portfolio managers or  362:24 those providing credit approval for  362:25 private label securities who read  363:1 prospectus supplements?  363:2 A. The whole, the whole  363:3 supplement?  363:4 Q. Yes.  363:5 A. No.</p>
<b>Hackney Tr. at 630:5 – 631:12</b>	<p>630:5 Q. (BY MS. DAVIDOFF) And my question was is  630:6 that your signature at the top of the trade ticket for  630:7 each of these trade tickets?  630:8 A. It is my signature on all but one.  630:9 Q. Which one is not your -- does not have your  630:10 signature?  630:11 A. The FHFA16863753.  630:12 Q. Okay. For the trade tickets that contain  630:13 your signature, does that indicate you reviewed the  630:14 trade ticket?  630:15 A. That -- that indicates that I was the trader.  630:16 Q. Okay. And do you recall anything  630:17 specifically about any of these deals?  630:18 A. I don't.  630:19 Q. Do you recall whether you reviewed the final  630:20 prospectus supplement?  630:21 A. I don't recall.  630:22 Q. Is there anything that would refresh your  630:23 recollection about that?  630:24 A. Not -- no.  630:25 Q. If your name is not on a trade ticket for a  631:1 deal, did you review or approve that trade?    631:3 A. It's unknown.  631:4 Q. (BY MS. DAVIDOFF) And how would you figure  631:5 that out?  631:6 A. You may not be able to.  631:7 Q. Okay. So it wouldn't necessarily appear  631:8 somewhere in the trade documentation if you had</p>



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	<p>631:9 reviewed the -- if you had reviewed or approved the 631:10 trade? 631:11 A. It would appear if I had approved. It would 631:12 not appear necessarily if I reviewed.</p>
<b>Henderson Tr. at 107:23-108:17</b>	<p>107:23 Do you know what a prospectus 107:24 supplement is? 107:25 A. I've heard of it. I don't  108:2 really know what it has in it. 108:3 Q. Okay. Do you know any 108:4 information that it contains? 108:5 A. Deal information. 108:6 Q. Have you ever read a prospectus 108:7 supplement? 108:8 A. No. 108:9 Q. So you didn't use prospectus 108:10 supplements in evaluating the nonagency trades 108:11 that you entered into, right?  108:16 A. As a trader, I personally 108:17 didn't read them.</p>
<b>Norris Tr. at 121:24 – 123:2</b>	<p>121:24 Q. 4.1.4 says "The dealer sends 121:25 the resulting pool characteristics and  122:2 the free writing prospectus, containing 122:3 the structure, collateral, and credit 122:4 enhancement of the deal. The dealer 122:5 sends a CDI file." 122:6 And then 4.1.5 says "The 122:7 nonagency mortgage trader verifies that 122:8 only approved issuers are in Fannie Mae's 122:9 class, referenced in the term sheet. If 122:10 an issuer is included that is unapproved, 122:11 the trader will ask the dealer to remove 122:12 this issuer's collateral from Fannie 122:13 Mae's class." 122:14 That portion of the process 122:15 verifying that approved issuers are in 122:16 Fannie Mae's class, is that something 122:17 that was done using the information sent 122:18 by the dealer that's described in 4.1.4? 122:19 A. Yes, this would be kind of as 122:20 we talked before, about the offering</p>

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	122:21 memorandum documentation. 122:22 Q. And when 4.1.5 describes 122:23 approved issuers being in Fannie Mae's 122:24 class, what is issuers referred to? 122:25 A. Issuers at this point in time  123:2 I believe referred to originators.

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<b>Kenneweg 30(b)(6) at 90:23 – 92:13</b>	<p>90:23 Q. Now, in this table, in Exhibit 90:24 1825, in Appendix A, there's reference to 90:25 approval authority. Right?</p> <p>91:2 A. There is. 91:3 Q. And it mentions the director of 91:4 institutional risk. Do you see that? 91:5 A. Mm-hmm. 91:6 Q. Yes or no. 91:7 A. Yes. I'm sorry. 91:8 Q. And who was the director of 91:9 institutional risk? 91:10 A. Pam Williams. I believe. I 91:11 have to go back and look. 91:12 I believe that's who that was 91:13 referring to. 91:14 Q. Okay. 91:15 A. But that's not her exact title 91:16 on the org chart. 91:17 Q. Okay. And did you understand 91:18 Ms. Williams to have certain counterparty 91:19 approval authority between 2005 and 2007? 91:20 A. That would be my understanding 91:21 from reading this chart. 91:22 Q. And which counterparties would 91:23 require Ms. Williams' approval? 91:24 A. Ones rated M-1 to M-3. 91:25 Q. Those are the higher rated --</p> <p>92:2 A. Right, yes. 92:3 Q. -- parties? 92:4 And then the director of CCRM, 92:5 was that Mr. Ratcliffe? 92:6 A. That would have been -- I 92:7 believe that's referring to Melissa Crabtree. 92:8 Q. And -- 92:9 A. Actually, at this time that 92:10 could have been -- at one point, at one point 92:11 he was director, and then he was vice 92:12 president. So I'm not -- I'm not exactly sure 92:13 now, going back, if this was Ron or Melissa.</p>
<b>Aneiro Tr. at</b>	252:1 Q. All right. I'd like to talk a

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252:1 to 255:24	<p>252:2 little bit about the credit analysis and</p> <p>252:3 credit approval we looked at earlier. I</p> <p>252:4 think that's in Exhibit 5206. We</p> <p>252:5 discussed that a credit approval was</p> <p>252:6 required for a typical PLS purchase in</p> <p>252:7 2005 to 2007?</p> <p>252:8 A. That's correct.</p> <p>252:10 Q. And who could provide a credit</p> <p>252:11 approval?</p> <p>252:12 A. The authorized people within</p> <p>252:13 the credit group.</p> <p>252:14 Q. Who were those?</p> <p>252:15 A. I don't recall the names, who</p> <p>252:16 was on the list.</p> <p>252:17 Q. Why was a credit approval</p> <p>252:18 required?</p> <p>252:19 A. Because there was credit risk</p> <p>252:20 associated with anything that's not</p> <p>252:21 considered a treasury bond and we needed</p> <p>252:22 credit approval, you know, to buy them.</p> <p>252:23 Q. What do you mean by credit</p> <p>252:24 risk?</p> <p>252:25 A. The risk of default.</p> <p>253:1 Q. And a credit approval was the</p> <p>253:2 result, was the -- was a credit approval</p> <p>253:3 the result of some kind of analysis?</p> <p>253:4 A. Correct.</p> <p>253:5 Q. And who conducted the credit</p> <p>253:6 analysis?</p> <p>253:7 A. The credit group.</p> <p>253:8 Q. What did a credit analysis</p> <p>253:9 entail?</p> <p>253:11 A. Counterparty risk including</p> <p>253:12 originator and servicer. Credit risk</p> <p>253:13 within the loans on an aggregated basis</p> <p>253:14 of the deal, level of subordination</p> <p>253:15 underneath our bond on a deal.</p> <p>253:16 Q. Anything else?</p> <p>253:17 A. Not that I can recall.</p> <p>253:18 Q. What did the analysis of</p> <p>253:19 counterparty risk -- what was the</p>

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253:20 analysis of counterparty risk?  
 253:21 A. We had a counterparty risk  
 253:22 group that would go out and review larger  
 253:23 counterparties, come up with various  
 253:24 ratings. We had a person within, within  
 253:25 investments in capital markets that was  
 254:1 the counterparty risk person that would  
 254:2 utilize those reports and evaluate the  
 254:3 credit risk on the counterparties, decide  
 254:4 whether to do business or not.  
 254:5 Q. Which counterparties were  
 254:6 reviewed for counterparty risk analysis?  
 254:7 A. Originators and servicers.  
 254:8 Q. Anybody else during 2005,  
 254:9 2006, 2007?  
 254:10 A. Insurance companies.  
 254:11 Q. Any other counterparties?  
 254:12 A. Not that I can remember.  
 254:13 Q. What did the -- what was the  
 254:14 process for providing a counterparty  
 254:15 analysis of originators in your  
 254:16 understanding?

254:19 A. It would be the group that  
 254:20 would go out and evaluate the business,  
 254:21 go to, go to the counterparty, evaluate  
 254:22 the practice, review their practice, come  
 254:23 back, write a report, rank them in  
 254:24 various ways and then confer with, or at  
 254:25 least provide that information to the  
 255:1 retained portfolios -- not the retained  
 255:2 portfolios, but ICM's counterparty risk  
 255:3 person, and she, in this case Stacey, but  
 255:4 she would use that to make a decision.  
 255:5 Q. Make a decision about what?  
 255:6 A. About approving the  
 255:7 counterparty for a deal.  
 255:8 Q. If a counterparty was  
 255:9 approved, what impact did that have?  
 255:10 A. It -- it allowed us to  
 255:11 purchase the bonds.  
 255:12 Q. So if an originator was an  
 255:13 approved counterparty, then a bond

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	<p>255:14 supported by collateral from that</p> <p>255:15 originator could be purchased, correct?</p> <p>255:17 A. That's one of the steps in</p> <p>255:18 credit evaluation.</p> <p>255:19 Q. Why was counterparty approval</p> <p>255:20 required before a PLS purchase could</p> <p>255:21 occur?</p> <p>255:22 A. Because the deals are</p> <p>255:23 dependent upon the performance of</p> <p>255:24 originators and servicers.</p>
<b>Bates Moss Tr. at 88:3 – 88:10</b>	<p>88:3 Q. Sure. The approvals that</p> <p>88:4 resulted from the counterparty reviews --</p> <p>88:5 A. Reviews.</p> <p>88:6 Q. -- that your group did, were</p> <p>88:7 those approvals then used by the people</p> <p>88:8 in trading to determine whether they</p> <p>88:9 could purchase a PLS on behalf of Fannie</p> <p>88:10 Mae?</p>
<b>Bates Moss Tr. at 88:13 – 88:21</b>	<p>88:13 A. Those approvals were used as a</p> <p>88:14 factor in determining whether or not they</p> <p>88:15 could move forward.</p> <p>88:16 Q. So the information that was</p> <p>88:17 collected by your group during the</p> <p>88:18 counterparty reviews was used in a</p> <p>88:19 process at Fannie Mae that ultimately</p> <p>88:20 resulted in the purchase of private label</p> <p>88:21 securities?</p>
<b>Bates Moss Tr. at 88:24 – 88:25</b>	<p>88:24 A. It could have resulted in the</p> <p>88:25 purchase.</p>
<b>Bates Moss Tr. at 89:2 – 89:11</b>	<p>89:2 Q. In fact, when traders bought</p> <p>89:3 private label securities on behalf of</p> <p>89:4 Fannie Mae, it was at the end of a</p> <p>89:5 process where after which your group had</p> <p>89:6 been involved in reviewing</p> <p>89:7 counterparties, collecting information</p> <p>89:8 about the counterparty and recommending</p> <p>89:9 approval or non-approval of doing a</p> <p>89:10 transaction with that counterparty,</p> <p>89:11 correct?</p>
<b>Bates Moss Tr. at 89:14 – 89:24</b>	<p>89:14 A. No.</p> <p>89:15 Q. Okay.</p> <p>89:16 A. Our role was to evaluate and</p>

Approval Authority for GSE PLS Purchases	
	<p>89:17 determine whether or not Fannie Mae could</p> <p>89:18 do business with the counterparty. It</p> <p>89:19 does not determine whether or not the</p> <p>89:20 actual transaction could be -- could move</p> <p>89:21 forward.</p> <p>89:22 Q. And so your step was the first</p> <p>89:23 step in the process by which Fannie Mae</p> <p>89:24 determined whether to purchase a PLS?</p>
<b>Bates Moss Tr. at 90:2 – 90:11</b>	<p>90:2 form.</p> <p>90:3 A. It is one step. Whether it's</p> <p>90:4 first or simultaneous, I don't know.</p> <p>90:5 Q. So your group's work in</p> <p>90:6 collecting information about a</p> <p>90:7 counterparty like an originator was one</p> <p>90:8 of the steps in a multi-step process by</p> <p>90:9 which Fannie Mae determined whether to</p> <p>90:10 purchase private label securities?</p> <p>90:11 A. That is correct.</p>
<b>Bates Moss Tr. at 739:7 – 739:16</b>	<p>739:7 Q. Right. And so if the</p> <p>739:8 counterparty credit risk group, which was</p> <p>739:9 your group --</p> <p>739:10 A. Yes.</p> <p>739:11 Q. -- did not approve an</p> <p>739:12 originator, a PLS trader at Fannie could</p> <p>739:13 not purchase from that originator unless</p> <p>739:14 they had approval from their business</p> <p>739:15 line, right?</p> <p>739:16 A. Yes.</p>

**GSE Use of Models in Pre-Purchase Analysis**

**Zhao Tr. at 74:2 -  
75:20**

74:2 Q. And did you talk at all at these Monday  
74:3 morning staff meetings prior to the third quarter of  
74:4 2006 about what you were going to do once you freed up  
74:5 from the restatement?

74:6 A. I don't think I talked at the staff meeting.  
74:7 I don't remember. I might have mentioned. But  
74:8 usually I also have biweekly one-on-one with Bill as  
74:9 his direct report. Usually -- actually, it probably  
74:10 only happen once a month because he was always too  
74:11 busy. So I would kind chat with him in terms of what  
74:12 I want to do, and sometimes I write e-mails.

74:13 Q. And what was it that you wanted to do?

74:14 A. In a nutshell, it's build a tool that can  
74:15 quan- -- use the base analytics that Fannie Mae  
74:16 already has or is going to develop to have a tool to  
74:17 quantify the credit risk of our PLS bonds.

74:18 THE REPORTER: "Our PLS" --

74:19 THE WITNESS: Bonds.

74:20 Q. (BY MR. SACCA) And that was something -- the  
74:21 tool could be used in connection with the purchase of  
74:22 PLS?

74:23 A. Yes.

74:25 Q. (BY MR. SACCA) And could it also be used in  
75:1 surveillance of PLS that Fannie owned?

75:2 A. Yes.

75:4 Q. (BY MR. SACCA) You said that you wanted the  
75:5 tool to use the base analytics that Fannie Mae already  
75:6 had or was going to develop.

75:7 What were those base analytics?

75:8 A. So Fannie, even at that point in late '05,  
75:9 being part of credit research team, I knew they  
75:10 actually already started estimating mod- -- default  
75:11 severity models for non-agency collaterals. And  
75:12 meanwhile, we also have another team developing home  
75:13 price forecast as well as a home price distribution.  
75:14 Then we have another team who does prepayment and the  
75:15 interest risk model, like term structure models.

75:16 So the idea is to put all of these  
75:17 together. And Francisco already had some code to do  
75:18 Intext analysis. So, you know, the first step for me



<b>GSE Use of Models in Pre-Purchase Analysis</b>	
	<p>75:19 was to put all these together so you truly have one 75:20 thing all in one tool.</p>
<b>Zhao Tr. at 76:15 -- 24</b>	<p>76:15 Q. (BY MR. SACCA) And who was it at Fannie Mae 76:16 that developed the home price forecasts? 76:17 A. The person I'm most familiar with -- again, 76:18 it's a legacy of model. It goes through lots of 76:19 versions; lots of people work on that. But the person 76:20 I'm most familiar with is Andre Gao. 76:21 Q. A-n-d-r-e? 76:22 A. Yeah. 76:23 Q. G-a-o? 76:24 A. Yeah.</p>
<b>Zhao Tr. at 95:19 -- 96:9</b>	<p>95:19 Q. Did you ever come to learn Fannie Mae's 95:20 corporate strategy with respect to PLS? 95:21 A. Other --  95:23 A. Other than I was told I need to hurry up and 95:24 finish building so that we can go buy some AA bonds. 95:25 That's kind of micro-level I know. Everything else I 96:1 don't think I was clear. 96:2 Q. (BY MR. SACCA) Okay. Who was it that told 96:3 you to hurry up and finish your model so Fannie Mae 96:4 could buy AA bonds? 96:5 A. I say that in a joking way. Nobody exactly 96:6 said those words -- 96:7 Q. Right. 96:8 A. -- but that's the idea. It's my boss, 96:9 Bill Quinn.</p>
<b>Zhao Tr. at 165:7 -- 166:25</b>	<p>165:7 Q. Item 1 under "Analytical Framework for PLS in 165:8 a nutshell" was to "Model underlying risk drivers: 165:9 home price and interest rate." 165:10 Were you proposing here to use the 165:11 Fannie Mae models or to do different modeling?  165:13 A. There -- there is both. I mean, most of the 165:14 stuff I want to use what's already there. Like here, 165:15 I also mention unemployment rate as potential risk 165:16 driver. At that point in Fannie Mae we didn't have a 165:17 model like that. So... 165:18 Q. (BY MR. SACCA) Okay. Were home price and 165:19 interest rate the two principal risk drivers for 165:20 private label securities?</p>

<b>GSE Use of Models in Pre-Purchase Analysis</b>	
	<p>165:21 A. In the model.</p> <p>165:23 A. Yes.</p> <p>165:24 Q. (BY MR. SACCA) And then you mentioned local</p> <p>165:25 unemployment rates. That's something that</p> <p>166:1 Fannie Mae's models did not capture at the time?</p> <p>166:2 A. That's correct.</p> <p>166:3 Q. And did there come a point in time when the</p> <p>166:4 models did capture local unemployment rates?</p> <p>166:5 A. No.</p> <p>166:6 Q. Do you know why not?</p> <p>166:7 A. A couple reasons. I rely on the research</p> <p>166:8 team to deliver the model. Nobody works -- worked on</p> <p>166:9 unemployment rate at that point. That's one.</p> <p>166:10 The second one, research at one point or</p> <p>166:11 another kind of showed me some chart to say once you</p> <p>166:12 account for home price interest rate, unemployment</p> <p>166:13 doesn't seem to be project -- and other -- other</p> <p>166:14 things in the model. Once you account -- whatever is</p> <p>166:15 in the model already, unemployment didn't improve the</p> <p>166:16 model fit or didn't add lots of explanatory power. So</p> <p>166:17 they didn't put on the priority list.</p> <p>166:18 Q. So research could test for what factors had</p> <p>166:19 explanatory power?</p> <p>166:20 A. There's some ways to test, yes.</p> <p>166:21 Q. And they'd share the results of those tests</p> <p>166:22 with you?</p> <p>166:24 A. At the one point or another it was definitely</p> <p>166:25 shared, yeah.</p>
<b>Zhao Tr. at 179:4 -- 181:4</b>	<p>179:4 (Deposition Exhibit 3508 marked.)</p> <p>179:5 (Document tendered.)</p> <p>179:6 Q. (BY MR. SACCA) 3508 bears production numbers</p> <p>179:7 FHFA01276322 through 44.</p> <p>179:8 Do you recognize the e-mail and its</p> <p>179:9 attachment?</p> <p>179:10 A. It's definitely my writing. Yes, I did write</p> <p>179:11 this. I -- I need time to really remember everything</p> <p>179:12 there, but I did write this.</p> <p>179:13 Q. Okay. Looking at the e-mail you sent on</p> <p>179:14 December 10th, 2006, at 10:15 p.m. to Mr. Quinn</p> <p>179:15 attaching the paper --</p> <p>179:16 A. Yeah.</p>

<b>GSE Use of Models in Pre-Purchase Analysis</b>	
	<p>179:17 Q. -- you say, "First of all, it seems that our  179:18 AAA bonds are truly 'unbreakable', if we have any  179:19 confidence in our internal analytics. What is my job  179:20 again?"</p> <p>179:21 What did you mean by that?</p> <p>179:22 A. It's meant to be a joke. That's why there's  179:23 smily face there.</p> <p>179:24 Well, I was hired to measure -- measure  179:25 more credit risk of that portfolio. If our internal  180:1 analytics always say the bond will never take a loss  180:2 in the worst case scenario, the home price model worst  180:3 case scenario, then they don't need me. They're  180:4 wasting my time.</p> <p>180:5 Q. Recognizing that you were joking here, it was  180:6 true, though, right, that when you ran bonds through  180:7 the Fannie Mae housing price model you could not break  180:8 AAA bonds, right?</p> <p>180:10 A. True. The bonds I ran -- and I don't know if  180:11 every single one passed every single test, but that's  180:12 the general conclusion.</p> <p>180:13 Q. (BY MR. SACCA) Right. Did any of the  180:14 Fannie Mae home price appreciation models you used in  180:15 2005, 2006, 2007 reflect what ultimately happened with  180:16 home price appreciation?</p> <p>180:17 A. Well, there was --</p> <p>180:19 A. There was definitely one or two prices like  180:20 that, but not -- not as our overall distribution. I  180:21 wouldn't characterize it that way.</p> <p>180:22 Q. (BY MR. SACCA) Okay. The Fannie Mae models  180:23 were more optimistic than what ultimately happened?</p> <p>180:24 A. Yes.</p> <p>181:1 Q. (BY MR. SACCA) And substantially so?</p> <p>181:3 A. Substantial? That's a vague word, but I  181:4 think yes.</p>
<b>Zhao Tr. at 181:24 -- 183:10</b>	<p>181:24 A. At least that's the model view.</p> <p>181:25 Q. You have a line near the bottom that starts,  182:1 "Fifth, who do we trust, our internal research people,  182:2 or rating agencies, or hearsay?"</p> <p>182:3 Do you see that?</p>

<b>GSE Use of Models in Pre-Purchase Analysis</b>	
	<p>182:4 A. Yeah.</p> <p>182:5 Q. Was -- was there a disconnect between what</p> <p>182:6 Fannie Mae's internal research was concluding versus</p> <p>182:7 what rating agencies were concluding or what you</p> <p>182:8 describe as hearsay?</p> <p>182:10 A. I don't know the detail about rating</p> <p>182:11 agencies. So for me to make a statement like that, it</p> <p>182:12 was almost like out of what I know. So in a way,</p> <p>182:13 it's -- it's not good sentiment on -- on my part.</p> <p>182:14 Hearsay -- hearsay I actually kind of</p> <p>182:15 remember. There -- at that point of time, end of</p> <p>182:16 2006, there were enough tracks in the news about a --</p> <p>182:17 about home price being too bubbled; things are going</p> <p>182:18 to turn south.</p> <p>182:19 Q. (BY MR. SACCA) So what you were hearing in</p> <p>182:20 the news was more pessimistic than Fannie Mae's</p> <p>182:21 internal models about home price appreciation would</p> <p>182:22 show?</p> <p>182:23 A. I don't think it's the mainstream news or</p> <p>182:24 anything. There were -- yes, there are some people</p> <p>182:25 saying that. So, you know, there are so many internet</p> <p>183:1 news, you have to pick which one you believe.</p> <p>183:2 Q. And this hearsay that you became aware of,</p> <p>183:3 was that something that you sought to incorporate into</p> <p>183:4 your credit risk model?</p> <p>183:5 A. No. It's not my job.</p> <p>183:6 Q. Okay. That's the modeling folks' job?</p> <p>183:7 A. Yeah.</p> <p>183:8 Q. Okay. Turning to your memo, would you -- is</p> <p>183:9 this what you would describe as a white paper?</p> <p>183:10 A. Yeah.</p>
<b>Zhao Tr. at 197:5 -- 16</b>	<p>197:5 Q. (BY MR. SACCA) So the stress scenarios you</p> <p>197:6 got from CRO, that came from them at some point after</p> <p>197:7 home prices started to decline?</p> <p>197:8 A. Definitely started to -- yeah. After.</p> <p>197:9 Q. Do you know when it was that the corporate</p> <p>197:10 approved Fannie Mae home price model caught up with</p> <p>197:11 the reality of home price movements?</p> <p>197:12 A. I don't know the --</p> <p>197:14 A. Yeah. I don't know the exact time. I know</p> <p>197:15 when things turned south they -- they worked much</p>

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	197:16 harder and faster. It became much more priority.
<b>Zhao Tr. at 389:9 -- 390:5</b>	<p>389:9 Q. (BY MR. BLUMENSTEIN) Okay. And what did  389:10 "CRO" stand for?  389:11 A. Chief Risk Office.  389:12 Q. So as of August 2007, Fannie was running  389:13 models using this stress scenario?  389:14 A. Yeah. Remember, this is a stress scenario.  389:15 Q. Uh-huh.  389:16 A. It's -- yeah.  389:17 Q. And this stress scenario called for home  389:18 price appreciation to drop by 10 percent during the  389:19 following two years and then remain level, is that  389:20 right?  389:21 A. Yeah.  389:22 Q. And, in fact, home price appreciation dropped  389:23 by more than 10 percent during the next two years,  389:24 correct?  389:25 A. It depends on the region. It depends on the  390:1 region.  390:2 Q. Do you know nationally, the national housing  390:3 price index?  390:4 A. I don't remember exact number, but around  390:5 those numbers, yeah.</p>
<b>Zhao Tr. at 390:15 -- 391:4</b>	<p>390:15 Q. (BY MR. BLUMENSTEIN) So under the CRO  390:16 scenario that we just described, almost all of Fannie  390:17 Mae's below AAA subprime bonds would be wiped out?  390:18 A. Yeah.  390:19 Q. Okay. Which is to say -- which means that  390:20 Fannie Mae understood by August 2007 that its below  390:21 AAA subprime PLS would be wiped out if the housing  390:22 market declined more than 10 percent over the next two  390:23 to three years?  390:25 A. When you say Fannie understood, it's -- it's  391:1 hard for me to agree to a general statement like that  391:2 because it's just what the model says. Whether Fannie  391:3 as a company agree or not would go through lots of  391:4 approval, lots of decision point, right?</p>
<b>Wood Tr. at 362:18 -- 363:2</b>	<p>362:18 Q. What do you mean by a statistical  362:19 measure of confidence in the AVM?  362:20 A. Again, it's an estimate. So based  362:21 on the input data going into a model, they will  362:22 have a certain level of confidence in the value</p>

<b>GSE Use of Models in Pre-Purchase Analysis</b>		
	362:23	coming out of that model. They will have been
	362:24	-- most models -- for example, on our model
	362:25	will indicate whether it's a high level or a
	363:2	medial level of confidence.
<b>Wood Tr. at 363:7 -- 15</b>	363:7	Q. And you said, "our model," I'm
	363:8	assuming Freddie Mac had its own?
	363:9	A. I'm sorry. Freddie Mac's
	363:10	proprietary model.
	363:11	Q. And that was called home value
	363:12	estimator?
	363:13	A. Yes.
	363:14	Q. It's also abbreviated HVE?
	363:15	A. Yes.
<b>Rosenblatt Tr. at 259:25 -- 261:12</b>	259:25	Q. Mr. Rosenblatt, one of the -- as I
	260:2	understood your testimony today, one of the
	260:3	functions of your group was to do loss modeling
	260:4	for loans on the single-family side; is that
	260:5	right?
	260:6	A. Yes, at different points -- yes.
	260:7	During many of these years, yes.
	260:8	Q. And in any of the -- and was one of
	260:9	the goals of doing these loss modeling to
	260:10	figure out what factors most influence the
	260:11	performance of loans, delinquencies, defaults
	260:12	and potential losses?
	260:14	THE WITNESS: Yes.
	260:15	BY MR. HARSCH:
	260:16	Q. And Fannie Mae would do its best to
	260:17	identify those factors that most affected loan
	260:18	performance through the loss modeling that your
	260:19	group would do?
	260:21	THE WITNESS: I mean, loss modeling
	260:22	is about estimating losses. It is not
	260:23	primarily about factors, but -- we discussed
	260:24	this before. It falls -- one could interpret
	260:25	from any of these models, sensitivities.
	261:2	BY MR. HARSCH:
	261:3	Q. And in any of the models that Fannie

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	<p>261:4 Mae developed while you were there in your  261:5 career, was one of the factors -- as part of  261:6 the models, was one of the factors affecting  261:7 loan performance, the degree to which any  261:8 originator had adhered to its underwriting  261:9 guidelines in originating the loan?</p> <p>261:11 THE WITNESS: I don't know that. I  261:12 don't think so</p>
<b>Vetrano Tr. at 192:12 -- 193:4</b>	<p>192:12 Q. And these were assumptions that  192:13 were built into DEFCAP. Correct?</p> <p>192:15 A. That's what the words say.  192:16 Q. What is DEFCAP?  192:17 A. DEFCAP was, might still be,  192:18 don't know, a credit evaluation model that was  192:19 used by Freddie Mac. It was designed for the  192:20 flow business. That was its primary use.  192:21 Credit model designed for flow business.  192:22 Q. So here Freddie Mac would  192:23 create some number of synthetic loans, apply  192:24 these assumptions, and then run them through  192:25 DEFCAP?</p> <p>193:3 A. That is apparently what the  193:4 words say.</p>
<b>Vetrano Tr. at 291:21 -- 24</b>	<p>290:21 Q. Do you see that the exceptions  290:22 for Alt-A are nearly seven times as high as  290:23 the exceptions for subprime?  290:24 A. I do see that.</p>
<b>Vetrano Tr. at 291:6 -- 23</b>	<p>291:6 Q. Sitting here today, why do you  291:7 think there's a disparity there?</p> <p>291:9 A. Freddie Mac's -- a potential  291:10 reason would be that Freddie Mac's internal  291:11 models viewed risk differently than the rating  291:12 agencies did.  291:13 Q. And that was more severe for  291:14 Alt-A than for subprime?</p> <p>291:16 A. There's more of a difference in  291:17 view as to what could be implied by that  291:18 statement.</p>



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	<p>291:19 Q. Anything else you can think of 291:20 that explains that disparity?</p> <p>291:22 A. We calibrated the process 291:23 incorrectly</p>
<b>Vetrano Tr. at 296:6 -- 298:11</b>	<p>296:6 Q. Did you feel that the model was 296:7 doing a good job, or did you feel that it was 296:8 off?</p> <p>296:10 A. A model is never accurate. 296:11 It's always providing a view. And so the 296:12 strict answer is there's not a product, 296:13 including 30-year or 15-year product, where I 296:14 thought the model was right.</p> <p>296:15 Q. What was your view of the risks 296:16 inherent in Alt-A product in 2006?</p> <p>296:17 A. The key risk is the same as you 296:18 have with every product. Maybe it's not 30 296:19 years, but at least to be able to see a 296:20 product through cycles, economic cycles. And 296:21 if you have a product that hasn't, where you 296:22 don't have the data to see what happened 296:23 through different economic cycles, there's 296:24 always a risk, always a heightened concern.</p> <p>296:25 Q. How would you address your</p> <p>297:2 heightened concern where you did not have 297:3 sufficient data to see how the collateral 297:4 would perform through economic cycles?</p> <p>297:6 A. That was pretty much the 297:7 description of the bulk process, and later the 297:8 PLS process. Almost by definition, the 297:9 products you're dealing with did not have a 297:10 history, so we did the best with the data we 297:11 had and made sure we understood how the model 297:12 came out with its results, and where the 297:13 strengths and weaknesses of those results 297:14 were.</p> <p>297:15 Q. Do you recall what the 297:16 strengths and weaknesses of the results were 297:17 for Alt-A collateral?</p> <p>297:18 A. I remember general concerns</p>



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	<p>297:19 that I had during that period, which pretty  297:20 much every risk person had during those  297:21 periods.  297:22 Q. What were those?  297:23 A. The sky is falling.  297:24 Q. What do you mean by that?  297:25 A. Every ABS conference we went to</p> <p>298:2 we say, This can't continue, and in every ABS  298:3 conference we would go to they would say, You  298:4 said that last year. That's the life of a  298:5 risk guy.  298:6 Q. What do you mean when you say  298:7 "this can't continue"?  298:8 A. Great performance. The market  298:9 had a view that was different than the risk  298:10 view. And pretty much the data substantiated  298:11 the market view.</p>
<b>Romano Tr. at 493:23 -- 495:18</b>	<p>493:23 Q. You were asked some questions  493:24 yesterday about the -- something called DEFCAP.  493:25 Do you recall that?</p> <p>494:2 A. Yes, I do.  494:3 Q. Okay. If you look through this  494:4 document, and I'll direct you to the second  494:5 paragraph on the second page, there is  494:6 mention -- and take a moment to look at it, but  494:7 there's mention of something called "subprime  494:8 DEFCAP model."  494:9 Do you see that?  494:10 A. I do.  494:11 Q. Okay. Does that refresh your  494:12 recollection about the use of something called  494:13 subprime DEFCAP at Freddie Mac?  494:14 A. I don't recall the details of how we  494:15 used that model.  494:16 Q. But you do recall that it was used  494:17 now?  494:18 A. I don't recall how it was used.  494:19 Q. But you do recall that it was used,  494:20 correct?  494:21 A. I recall that there was a model  494:22 called subprime DEFCAP, but I don't recall how</p>

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	<p>494:23 it was used.</p> <p>494:24 Q. If you look at the last paragraph on</p> <p>494:25 that page beginning with the word "first,</p> <p>495:2 first, the subprime matrixes are derived from</p> <p>495:3 the most up-to-date DEFCAP subprime model,</p> <p>495:4 Version 7.4, while Alt-A matrixes are still</p> <p>495:5 based on an outdated version. In the monthly</p> <p>495:6 MABS meeting in May 2006, modeling group agreed</p> <p>495:7 to deliver the updated Alt-A matrixes by the</p> <p>495:8 end of June."</p> <p>495:9 Do you see that?</p> <p>495:10 A. I do.</p> <p>495:11 Q. Does this refresh your recollection</p> <p>495:12 that the subprime DEFCAP model was used with</p> <p>495:13 respect to MABS or private label security</p> <p>495:14 transactions?</p> <p>495:15 A. I can read what it says. I don't</p> <p>495:16 recall exactly how we used that model. I have</p> <p>495:17 no reason to believe this information is not --</p> <p>495:18 not accurate.</p>
<b>Palmer Tr. at 160:14 -- 161:5</b>	<p>160:14 Q. But that was not, I take it,</p> <p>160:15 part of the DEFCAP analysis we've just</p> <p>160:16 read about?</p> <p>160:18 Q. Or was it?</p> <p>160:20 A. DEFCAP did not have an</p> <p>160:21 originator or aggregator issuer input</p> <p>160:22 into that model.</p> <p>160:23 Q. And did it have an input that</p> <p>160:24 was designed to capture Freddie Mac's</p> <p>160:25 perception regarding whether the loans</p> <p>161:2 had been underwritten according to the</p> <p>161:3 originator's guidelines?</p> <p>161:5 A. No.</p>
<b>Palmer Tr. at 646:17 -- 650:7</b>	<p>646:17 Q. Yesterday you talked about</p> <p>646:18 some of the inputs that went into the</p> <p>646:19 subprime DEFCAP matrix and I want to just</p> <p>646:20 clarify. Why don't we take a look at one</p> <p>646:21 your credit approval letters. It was --</p>

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646:22 or memos. It was previously marked as  
 646:23 Exhibit 5203 and ask if you could take a  
 646:24 look at that.  
 646:25 If you turn to the second page

647:2 that has the credit approved on top and  
 647:3 then it has a series of collateral info  
 647:4 metrics, beginning with weighted average  
 647:5 FICO, if you could look at those, if you  
 647:6 could go through each one and tell me  
 647:7 whether or not each of those  
 647:8 characteristics were inputs in the  
 647:9 subprime DEFCAP model?

647:11 A. The DEFCAP matrices or the  
 647:12 DEFCAP model?  
 647:13 Q. The DEFCAP -- well, either.  
 647:14 A. Okay.

647:17 DEFCAP model and the DEFCAP matrices.  
 647:18 That also covers FICO less than 600.  
 647:19 CLTV was an input into the DEFCAP model  
 647:20 and an input into the DEFCAP matrices,  
 647:21 which includes the next three rows all  
 647:22 the way down to greater than 80 CLTV.  
 647:23 Full doc was an input into the  
 647:24 DEFCAP model as well as the DEFCAP  
 647:25 matrices.

648:2 Owner occupied was an input  
 648:3 into the DEFCAP model. It was not an  
 648:4 input directly into the DEFCAP matrices.  
 648:5 Two to four unit property was  
 648:6 an input into the DEFCAP model. It was  
 648:7 not an input directly into the DEFCAP  
 648:8 matrices.  
 648:9 Cashout refinance was an input  
 648:10 into the DEFCAP model. It was not an  
 648:11 input directly into the DEFCAP matrices.  
 648:12 IO/MTA, or interest only  
 648:13 option ARM loans, was an input into the  
 648:14 DEFCAP model. It was also an input into  
 648:15 the DEFCAP matrices.

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	<p>648:16 California, or the state in  648:17 which the loan resided was an input into  648:18 the DEFCAP model. It was not directly an  648:19 input into the DEFCAP matrices.</p> <p>648:20 Q. And you referred to, we saw  648:21 some documents that talked about the  648:22 output of the DEFCAP matrix referring to  648:23 the 300th path and whether or not there  648:24 would be costs associated with the 300th  648:25 path. In layman's terms, can you just</p> <p>649:2 explain what that is? Is that like a, is  649:3 it fair to say that would be like a worst  649:4 case scenario would be represented by  649:5 300th path assuming the various inputs  649:6 like interest rates and the like?</p> <p>649:8 A. This is -- this is more of a  649:9 modeling question which is not my  649:10 background. Each of the 300 paths  649:11 represented a different home price and  649:12 interest rate scenario that had an equal  649:13 probability of occurring. And we would  649:14 look at, this was the same process, you  649:15 know, or practice that took place in  649:16 modeling other single family mortgages at  649:17 Freddie Mac, and we would use that to  649:18 estimate what the credit costs were on  649:19 single family loans and then as a  649:20 creation of the DEFCAP matrices,  649:21 estimating what the credit costs may be  649:22 on AAA purchases.</p> <p>649:23 Q. And I take it with the DEFCAP  649:24 matrices you wouldn't know whether there  649:25 would be a credit cost by looking at any</p> <p>650:2 particular loan characteristic in  650:3 isolation, right, like FICO score, until  650:4 you ran the matrix?</p> <p>650:6 A. You needed to look at the  650:7 whole picture.</p>
<b>Palmer Tr. at</b>	654:24 Q. Do you know whether the models

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<b>654:24 -- 655:18</b>	<p>654:25 that Freddie Mac used to determine credit</p> <p>655:2 risk was any more or less sophisticated</p> <p>655:3 than the models or tools that were</p> <p>655:4 available to other investors in PLS in</p> <p>655:5 the 2005 to 2007 time period?</p> <p>655:6 A. I don't know.</p> <p>655:7 Q. You don't have any views one</p> <p>655:8 way or the other?</p> <p>655:9 A. No.</p> <p>655:10 Q. Were you aware that when</p> <p>655:11 Freddie Mac was placed into</p> <p>655:12 conservatorship in 2008 one of the</p> <p>655:13 criticisms of the regulators was that</p> <p>655:14 Freddie Mac had unsafe and unsound</p> <p>655:15 practices concerning its use of models?</p> <p>655:16 Were you aware of that?</p> <p>655:17 A. I believe, I believe I was</p> <p>655:18 aware of that.</p>
<b>Mudd Tr. at 245:21 -- 22; 246:2 -- 20</b>	<p>245:21 Q Did you in Fannie Mae have models to</p> <p>245:22 predict performance of the housing market?</p> <p>246:2 A Yes, there were mod- -- there were home</p> <p>246:3 price models at Fannie Mae.</p> <p>246:4 Q And did the home price models at Fannie</p> <p>246:5 Mae accurately predict the 30 percent</p> <p>246:6 peak-to-trough decline that, in fact, came to</p> <p>246:7 pass?</p> <p>246:8 A No.</p> <p>246:9 Q And would you agree that your -- that</p> <p>246:10 everybody's models, including ours, Fannie Mae's,</p> <p>246:11 undershot the severity of what occurred in the</p> <p>246:12 marketplace?</p> <p>246:15 THE WITNESS: The models that I'm aware</p> <p>246:16 of un-predict- -- under predicted.</p> <p>246:17 BY MR. STARK::</p> <p>246:18 Q Under predicted the severity of the</p> <p>246:19 decline in house prices?</p> <p>246:20 A Yes.</p>
<b>Corley 30(b)(6) Tr. at 380:2 -- 381:14</b>	<p>380:2 Q. Who analyzes loans?</p> <p>380:3 A. The Freddie Mac single-family</p> <p>380:4 costing team.</p>

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380:5	Q. And is that model used anywhere else
380:6	in Freddie Mac, or just in single-family?
380:8	THE WITNESS: It's referring to
380:9	DEFCAP, which I think we have talked about in
380:10	prior depositions. There are different areas
380:11	of the company that used DEFCAP for different
380:12	purposes, but it wouldn't have been in -- used
380:13	at the loan level for -- by the portfolio
380:14	managers.
380:15	BY MR. BATHAEE:
380:16	Q. Do you recall DEFCAP being used in
380:17	conjunction with PLS?
380:20	THE WITNESS: That was part of my
380:21	prior deposition, but again, it wasn't used at
380:22	the loan-level basis. It was -- a modified
380:23	version of it was -- or tried to take
380:24	characteristics or general buckets of
380:25	characteristics that made up PLS securities to
381:2	try to approximate how much credit enhancement
381:3	we thought was adequate for PLS deals.
381:4	BY MR. BATHAEE:
381:5	Q. And for PLS deals, DEFCAP would take
381:6	into account your cost of capital on a
381:7	risk-adjusted basis?
381:9	THE WITNESS: For PLS deals, did it
381:10	take into account?
381:11	I'm not sure if that element of
381:12	DEFCAP was used. PLS trades had their own ROE
381:13	and their own capital spreadsheet that was
381:14	used.
<b>Hackney Tr. at 68:11 -- 69:10</b>	68:11 Q. What -- what sort of analysis, if any, did
	68:12 you run on the collateral stratifications you
	68:13 received?
	68:15 A. Define what you mean by "analysis."
	68:16 Q. (BY MR. SACCA) Did you plug the
	68:17 stratifications into any model or tool you used?
	68:18 A. Yes.
	68:19 Q. Okay. Which models or tools?

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	<p>68:20 A. If they had produced a CDI, then I would plug  68:21 that into our proprietary Freddie Mac model. I may  68:22 also have utilized Intex to look at the security.  68:23 Q. And what's a CDI?  68:24 A. It's a waterfall structure.  68:25 Q. And is that something you would typically  69:1 receive from dealers at the time you received the  69:2 initial collateral stratifications?  69:3 A. Not necessarily. There could be many ongoing  69:4 conversations back and forth. Some dealers felt that  69:5 they had a pretty good understanding of what it would  69:6 take to create a security that people would be  69:7 interested in. Others wanted much more feedback, so  69:8 they do -- they get a pool of loans and without doing  69:9 anything start asking for some feedback, such as are  69:10 these loans charter eligible.</p>
<b>Kain Tr. at 283:4 -- 12</b>	<p>283:4 Q. And did you know that DEFCAP's  283:5 models are -- internal models are based on the  283:6 performance of loans on the single-family side?</p> <p>283:8 THE WITNESS: That is my  283:9 recollection, yes.  283:10 BY MR. BENNETT:  283:11 Q. So is it your recollection then that  283:12 at some point, and I know you don't know  283:13 exactly the time, Freddie Mac was using models  283:14 based on the performance of loans on the  283:15 single-family side to assess the credit risk on  283:16 the PLS side of the business?</p> <p>283:18 THE WITNESS: Can you repeat the  283:19 question?  283:20 BY MR. BENNETT:  283:21 Q. Sure. So was it your understanding  283:22 that Freddie Mac used models based on the  283:23 performance of loans from the single-family  283:24 side to assess the credit in the PLS portfolio?</p> <p>284:1 GARY KAIN  284:2 THE WITNESS: It appears from  284:3 looking at this, that that seems to be the  284:4 case. I don't know how often DEFCAP was used.  284:5 I know it wasn't the main tool for that</p>

<b>GSE Use of Models in Pre-Purchase Analysis</b>	
	<p>284:6 analysis most of the time.  284:7 BY MR. BENNETT:  284:8 Q. What was the main tool for that  284:9 analysis most of the time?  284:10 A. I think there was more of a  284:11 spreadsheet-based approach, but I'm, you know,  284:12 not sure.</p>
<b>P. Cook Tr. at 279:15 -- 21</b>	<p>279:15 Q Were your models in February 2007  279:16 accurately predicting house price appreciation as  279:17 it would later come to pass?</p> <p>279:19 THE WITNESS: No, I don't think any  279:20 model was correctly predicting a single accurate  279:21 path for house prices.</p>
<b>P. Cook Tr. at 297:15 -- 25</b>	<p>297:15 Q I think you testified about this  297:16 earlier, but either through your models or  297:17 otherwise, Freddie Mac -- nobody at Freddie Mac,  297:18 as far as you're aware, predicted the magnitude of  297:19 the house price decline that actually came to pass  297:20 in the 2007 -- latter half of 2007 and 2008 time  297:21 period; right?</p> <p>297:24 THE WITNESS: I don't -- we didn't  297:25 predict the path for house prices.</p>
<b>Cao Tr. at 686:15 -- 687:10</b>	<p>686:15 At that time, you didn't factor into  686:16 Fannie Mae's models any factors that had to do  686:17 with the degree to which Fannie Mae thought  686:18 that these originators adhered to underwriting  686:19 guidelines, correct?</p> <p>686:21 THE WITNESS: It's kind of -- it's a  686:22 work that is being done by another firm. You  686:23 know, it is always like -- the whole thing, you  686:24 know, everybody has their roles to reform  686:25 liquidity. You know, whatever some people</p> <p>687:2 underwritten data, and then we bought them and  687:3 then you want us to re-underwrite everything.  687:4 That is not Fannie Mae's role, right, and then  687:5 this loan, actually, this nonperforming loans,  687:6 they are not PLS. Actually, it's kind of  687:7 funny.  687:8 The nonperforming loans are the ones</p>



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	<p>687:9 that Fannie Mae actually had bought and then</p> <p>687:10 become nonperforming.</p>
<b>Cao Tr. at 689:4-690:12</b>	<p>689:4 Q. For the most part, when these loans</p> <p>689:5 were originated, it was the originators that</p> <p>689:6 was responsible for originating them in</p> <p>689:7 accordance with the guidelines that Fannie Mae</p> <p>689:8 set, correct?</p> <p>689:10 THE WITNESS: I believe so.</p> <p>689:11 BY MR. HARSCH:</p> <p>689:12 Q. So now in the models that you ran to</p> <p>689:13 determine the intrinsic value of these</p> <p>689:14 mortgages, did Fannie Mae incorporate any</p> <p>689:15 variables that reflected the degree to which</p> <p>689:16 Fannie Mae felt that these originators had</p> <p>689:17 adhered to the guidelines to which these loans</p> <p>689:18 were supposed to have been originated?</p> <p>689:20 THE WITNESS: Not we ran</p> <p>689:21 underwriting it? We underwrite it or -- we do</p> <p>689:22 have called, you know, getting to the model</p> <p>689:23 components, we have an ACI model which is kind</p> <p>689:24 of super-FICO kind of index we created, based</p> <p>689:25 on the borrower information that actually have</p> <p>690:2 all this borrower-specific information, FICOs,</p> <p>690:3 and all that information, income, TDI, LTV, all</p> <p>690:4 fits into it, and then we would come out with,</p> <p>690:5 like, we call them super-FICO. So it's helped</p> <p>690:6 to identify the risk of the borrowers, so we</p> <p>690:7 never really -- I mean, under -- we ran -- the</p> <p>690:8 underwriting was not in the model, right.</p> <p>690:9 BY MR. HARSCH:</p> <p>690:10 Q. The underwriting was not in the</p> <p>690:11 model?</p> <p>690:12 A. No.</p>
<b>Cao Tr. at 691:15 -- 21</b>	<p>691:15 Q. In those models, was there any</p> <p>691:16 variable that accounted for the degree to which</p> <p>691:17 Fannie Mae had concluded that the originators</p> <p>691:18 adhered to the underwriting guidelines that</p> <p>691:19 they were supposed to adhere to in originating</p> <p>691:20 these loans?</p> <p>691:21 A. Not that I am aware of.</p>

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<b>Cao Tr. at 692:3 - 22</b>	692:3	Q. Did you apply any similar models in
	692:4	evaluating PLS?
	692:6	THE WITNESS: Not the same model.
	692:7	BY MR. HARSCH:
	692:8	Q. Similar model?
	692:9	A. Not the same model at the time.
	692:10	There is totally different versions of models
	692:11	right now.
	692:12	Q. Did you apply models that projected
	692:13	the anticipated performance of loans that
	692:14	underlie PLS?
	692:16	THE WITNESS: Yes.
	692:17	BY MR. HARSCH:
	692:18	Q. Did any of those models take into
	692:19	account any variables to reflect the degree
	692:20	which Fannie Mae had concluded that originators
	692:21	adhered to underwriting guidelines?
	692:22	A. Not that I'm aware of.
<b>Bisenius Tr. at 44:8 -- 45:13</b>	44:8	And you said you picked up responsibility
	44:9	for the analytical models. Do you know what models in
	44:10	particular you picked up responsibility for?
	44:11	A As best I recall, it would have included
	44:12	Loan Prospector. I don't believe at that time it
	44:13	included DEFCAP, which was the default costing model,
	44:14	and there may have been others. I just don't recall.
	44:15	Q What were your responsibilities with respect
	44:16	to Loan Prospector? Were you -- I take it you weren't
	44:17	hands-on programming Loan Prospector, right?
	44:18	A That is correct.
	44:19	Q So what did you do with respect to Loan
	44:20	Prospector in terms of your -- well, your
	44:21	responsibilities at that time?
	44:22	A I would have been responsible for setting,
	44:23	kind of, the overall direction for -- for the model,
	44:24	both its development and its use within the business.
	44:25	Q When you say setting the overall
	45:2	direction -- well, can you describe what Loan
	45:3	Prospector does?
	45:4	A Sure, Loan Prospector is a statistical model
	45:5	designed to, kind of, predict the probability --

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	<p>45:6 actually, designed to create a relative rank ordering  45:7 of the risks of the mortgages that were being  45:8 evaluated.</p> <p>45:9 Q And is Loan Prospector a tool that loan  45:10 originators or sellers can use to determine whether a  45:11 loan will qualify for Freddie Mac's -- under Freddie  45:12 Mac's underwriting requirements?  45:13 A Yes.</p>
<b>Bisenius Tr. at 284:23 -- 287:11</b>	<p>284:23 Q If you turn in your set of documents to  284:24 Exhibit 35603.  284:25 A Yes.</p> <p>285:2 Q And this is a memo from Mr. Vetrano to  285:3 yourself concerning "proposed new process to analyze  285:4 MABS credit structure risk."  285:5 A Okay.</p> <p>285:6 Q And do you recall looking at the org chart  285:7 earlier, at this time, Mr. Vetrano reported directly  285:8 to you?  285:9 A If you give me a reference, I can confirm  285:10 that.</p> <p>285:11 Q Yes, sorry. That is Exhibit 602, or it ends  285:12 in 602. 35602.  285:13 A Yes, I see that, okay. Yes.</p> <p>285:14 Q So the person who reports directly to you is  285:15 proposing a new process to analyze MABS credit  285:16 structure. Regardless of whether you recall this  285:17 particular memo, what would be your practice with  285:18 respect to reviewing or commenting on such proposals  285:19 by a direct report to you?</p> <p>285:21 A It's a broad question. I appreciate that.  285:22 As a general matter, if I was being asked to approve a  285:23 policy, I would review the policy, probably discuss it  285:24 with the person proposing it and either run it through  285:25 an approval process, which most policies required, and</p> <p>286:2 get either approved or denied.</p> <p>286:3 Q So turning back to Exhibit 35603, do you  286:4 recall having a discussion with Mr. Vetrano about this  286:5 proposed new process?</p> <p>286:7 A I don't recall a conversation on it.</p>

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	<p>286:8 Q I think we discussed earlier Mr. Vetrano  286:9 testified that he recalled you asking him to develop a  286:10 process for analyzing MABS credit structures that  286:11 would create a process that would be consistent in  286:12 analyzing MABS in the same way that Freddie Mac  286:13 analyzed the bulk loans being bought through the bulk  286:14 process.  286:15 Do you have a recollection of giving him  286:16 that direction?  286:17 A No, I don't.</p> <p>286:19 Q If you turn to the second page of the  286:20 document, Bates labeled 227. This is of Exhibit  286:21 35603.  286:22 A 603, yes.  286:23 Q Setting aside this particular memo, which  286:24 you may or may not recall, do you recall that  286:25 generally the credit review process for PLS purchases    287:2 used the DEFCAP model to try to estimate projected  287:3 losses from loans underlying the securitization?    287:5 A What I recall in looking at this one,  287:6 actually helps refresh it, is I think they were trying  287:7 to figure out a way to use the DEFCAP model to  287:8 evaluate those portfolios, but I think it was -- my  287:9 recollection is that it wasn't designed specifically  287:10 to do that and so there was an attempt to see if it  287:11 could be used.</p>
<b>Bisenius Tr. at 288:2 -- 290:15</b>	<p>288:2 Q So having read the memo, does that refresh  288:3 your recollection about the process that was being  288:4 attempted to be used to use DEFCAP to help to value  288:5 the credit underlying MABS portfolio purposes?    288:7 A As I look at this, I recall there being  288:8 conversations around doing this one, yes.  288:9 Q Great.  288:10 Maybe let's just start with, what do you  288:11 recall about the conversations?  288:12 A Pretty much what's summarized in the memo  288:13 itself, which was recognizing that DEFCAP was not  288:14 designed for pools, it was designed for loan-level  288:15 type analysis, was there a way that we could use</p>

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288:16 pool-type stratifications and still capture them  
 288:17 within DEFCAP. I also recall there being a discussion  
 288:18 about kind of a level of information that Freddie Mac  
 288:19 received prior to its purchase of private label  
 288:20 securities and whether that information needed to be  
 288:21 expanded to be able to allow them to use the DEFCAP  
 288:22 type model.

288:23 Q So you recall that there was a proposal to  
 288:24 require dealers to provide breakdowns of their pool by  
 288:25 FICO/LTV buckets?

289:2 A That's -- as this thing suggests, that's my  
 289:3 recollection.

289:4 Q And then there would also be 12 FICO/LTV  
 289:5 grids which would be used to evaluate those pools; is  
 289:6 that correct?

289:8 A Again, as the memo describes, I didn't  
 289:9 recall the 12, but it says 12, that makes sense.

289:10 Q Right.

289:11 Do you recall then that those grids would be  
 289:12 populated in terms of expected loss by running the  
 289:13 DEFCAP model?

289:15 A Again, that's my general recollection having  
 289:16 read this. That's right.

289:17 Q And do you recall that they would run the  
 289:18 DEFCAP model at different levels, at the 50 percent,  
 289:19 the 99 percent, the 100 percent, to see what losses  
 289:20 would be projected under each of the different  
 289:21 scenarios under DEFCAP?

289:23 A I don't recall that specifically. I know  
 289:24 there was some desire -- because, again, we're talking  
 289:25 about the investment in the retained portfolio. It's

290:2 not as much about the loan level as it is about the  
 290:3 subordination level and the, kind of, risk of the  
 290:4 structure. I think that's what they were trying to do  
 290:5 for the risk of the structure, but I don't have as  
 290:6 clear of a recollection on that.

290:7 Q Right. And so, generally, do you understand  
 290:8 the idea was to estimate the risk of potential losses

<b>GSE Use of Models in Pre-Purchase Analysis</b>	
	<p>290:9 using the DEFCAP model and then figure out whether the</p> <p>290:10 credit enhancements that were provided in the security</p> <p>290:11 structure would be sufficient to protect against that</p> <p>290:12 level of losses?</p> <p>290:14 A That's my understanding of what they were</p> <p>290:15 trying to do, that's right.</p>
<b>Bisenius Tr. at 299:6 -- 299:14</b>	<p>299:6 Q When you say when you look at this</p> <p>299:7 particular, would that be an area where you would have</p> <p>299:8 some concern concerning the averages that were used as</p> <p>299:9 the DEFCAP model?</p> <p>299:11 A My concern actually consists with how it's</p> <p>299:12 articulated here, that is if the deal has</p> <p>299:13 characteristics that are different or exceed what the</p> <p>299:14 average assumptions were, it's going to be riskier.</p>
<b>Bisenius Tr. at 304:12 -- 305:8</b>	<p>304:12 Q On page 820, the first page, the last</p> <p>304:13 paragraph of the summary, he says, "This exercise</p> <p>304:14 suggests the new MABS credit process will reduce</p> <p>304:15 operational risk but increase exposure to model risk."</p> <p>304:16 Do you see that?</p> <p>304:17 A Uh-hmm.</p> <p>304:18 Q Did you have an understanding of what</p> <p>304:19 Prospector Vetrano meant by model risk at the time?</p> <p>304:20 A I have an understanding of what model risk</p> <p>304:21 is. I don't know whether this is what Frank was</p> <p>304:22 meaning when he wrote those words. So I can describe</p> <p>304:23 what my understanding of model risk is.</p> <p>304:24 Q Yes, if you would.</p> <p>304:25 A It's that the model -- the estimates of the</p> <p>305:2 coefficients in the model are, for some reason, not</p> <p>305:3 applicable to the population of loans that you're</p> <p>305:4 applying it to. So models are built off of a core</p> <p>305:5 dataset. If the pool of loans, the group of loans</p> <p>305:6 that the model results are being applied to is</p> <p>305:7 inconsistent with what the model was built on, you</p> <p>305:8 could have model risk.</p>
<b>Bisenius Tr. at 305:21 -- 306:16</b>	<p>305:21 Generally if the model assumed information</p> <p>305:22 that was different from what was included in the</p> <p>305:23 underlying pool, that's another example of model risk</p> <p>305:24 where the model could project a set of losses that</p> <p>305:25 would be different from what would actually happen</p>

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	<p>306:2 with the underlying pool?</p> <p>306:4 A Yes, as you described that, I don't know if  306:5 I thought of that as model risk. So it could be. The  306:6 way I think about it is a model is being used on a  306:7 group of loans different than what it was built on, so  306:8 I think of model risk.</p> <p>306:9 Q But you would agree generally there's a risk  306:10 if the -- if the model is using a set of assumptions  306:11 that is inconsistent with what the underlying pool  306:12 actually contains, that the model might misestimate  306:13 the risk of loss?</p> <p>306:15 A I believe that's a risk. I just don't know  306:16 whether I would label it a model risk.</p>
<p><b>Vetrano Tr. at  422:17 -- 424:23</b></p>	<p>422:17 Q. The sentence then goes on to  422:18 say: "We need to remain wary of blind spots  422:19 in our models."  422:20 Do you see that?</p> <p>422:21 A. I see that.</p> <p>422:22 Q. Do you know what you mean by  422:23 "blind spots" in your models?</p> <p>422:24 A. I don't recall the context  422:25 within which this was written.</p> <p>423:2 Q. Okay. Regardless of whether  423:3 you recall the context in which this is  423:4 written, is it fair to say that a blind spot  423:5 in a model is a place in the model where  423:6 you're making assumptions or making decisions,  423:7 but you don't know information that might  423:8 exist out in the real world?</p> <p>423:10 A. That's a possible result.</p> <p>423:11 Q. Is there any other definition  423:12 of a blind spot in the model that you would  423:13 have, sitting here today?</p> <p>423:15 A. As we did discuss yesterday,  423:16 the DEFCAP model was designed around 30 or 40  423:17 years of data, and we were using best  423:18 information available for this purpose for</p>



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	<p>423:19 which we did not have 30 or 40 years of data.  423:20 I would guess that one possibility is a  423:21 recognition that we did not have 30 or 40  423:22 years of data for this model, and therefore  423:23 needed to be cautious about what the results  423:24 said.  423:25 Q. You said that DEFCAP used 30 to</p> <p>424:2 40 years of data. Do you know what 30 to 40  424:3 years it looked at?  424:4 A. Freddie Mac's history of  424:5 single-family 30-year, 15-year data, is what  424:6 the model was honed on.  424:7 Q. Sorry. When you say 30-year  424:8 and 15-year data, those sound to me like  424:9 durations of mortgages. Is that -- are you  424:10 saying that you based the DEFCAP model on  424:11 Freddie Mac's experience with 30-year mortgage  424:12 products?</p> <p>424:14 A. The original use of the DEFCAP  424:15 model was to evaluate the risk of its generic  424:16 business, which was comprised primarily of  424:17 30-year fixed-rate mortgages and 15-year  424:18 fixed-rate mortgages. The calibrations of the  424:19 model incorporated experience from as far back  424:20 as Freddie Mac's data goes, and I am not sure  424:21 how far it goes back, hence my 30 to 40 years.  424:22 I am guessing. And that was the origins and  424:23 the primary use of the model.</p>
<b>Cao Tr. at 240:2 - 242:16; 243:9 -- 24</b>	<p>240:2 Q. At some point, Fannie Mae stopped  240:3 the pre-settlement checklist process in favor  240:4 of a different kind of analysis; is that  240:5 correct?  240:6 A. Yes.  240:7 Q. And that's what you described as CJ  240:8 Zhao's model?  240:9 A. Correct.  240:10 Q. And describe for me, please, the  240:11 difference between the two approaches?</p> <p>240:13 THE WITNESS: Pre-settlement, you  240:14 can say that it's just a very simple</p>



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240:15 240:16 240:17 240:18 240:19 240:20 240:21 240:22 240:23 240:24 240:25  241:2 241:3 241:4 241:5 241:6 241:7  241:9 241:10 241:11 241:12 241:13 241:14 241:15 241:16 241:17 241:18 241:19 241:20 241:21 241:22  241:24 241:25  242:2 242:3 242:4 242:5 242:6 242:7	spreadsheet, one page or two of, you know, checking of the invention at the time, right. CJ's model is a stochastic model and then used on other data as input and then collect the cash flow with deal structure throughout the model. So below that, all the information with all the embedded risk factors requested by the model and fit into the process, generally the cash flow, by doing, you know, simulations based on home price interest rates environment and then generated cash flow based on that and  then run through the cash flow, you know, through the INTEx, you know, the structure of the deal and then estimate the credit risks and estimate the loss of the bonds and the price of the bonds based on the -- you know, per model. Q. What is a stochastic model?  THE WITNESS: Basically using simulation approach to simulate your different -- the key inputs and then outputs the -- you know, different kind of results. So it's kind of probably realistic -- real. BY MR. SACCA: Q. And did you say inputs into the model included loan level data? A. That's required. Loan level, yes. Q. And the loan level data that Fannie Mae put into the model was loan level data specific to the particular deal you were modeling? A. Yes.  BY MR. SACCA: Q. And from where did you get the data?  A. From the issuer, the dealer. Q. And did that come from the loan tape or the CDI file or -- A. Low level data is from loan tape. The structure is from CDI. Q. And what sort of loan level data
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<b>GSE Use of Models in Pre-Purchase Analysis</b>		
	242:8	went into the model?
	242:10	THE WITNESS: Again, there are a lot
	242:11	of fields that in the data table -- I think we
	242:12	went through this this morning, so not remember
	242:13	every single thing, but, you know, LTV, FICO,
	242:14	coupon, you know, note rates, specifically, and
	242:15	then seasoning, how long season, and then
	242:16	geography. That's, you know, the gist of it.
	....	
	243:10	Q. Why did the CMS group switch from
	243:11	the pre-settlement checklist model to the CJ
	243:12	Zhao model?
	243:13	A. Because then this model give us
	243:14	wholistic view of the risk and return.
	243:15	Q. So you thought it would do a better
	243:16	job of assessing risk?
	243:17	A. Definitely.
	243:18	Q. Did you perceive that the
	243:19	pre-settlement checklist process didn't
	243:20	accurately capture risk?
	243:22	THE WITNESS: It's -- I wouldn't say
	243:23	it's not accurate. It's just limited compared
	243:24	to this more extensive model.
<b>Cao Tr. at 89:16 - - 91:2</b>	89:16	THE WITNESS: We have credit risk
	89:17	policy and we have steps. For my job, I relied
	89:18	on what the model tells me, so we have internal
	89:19	model and then we have Intex which are actually
	89:20	linked to Intex in the internal model. It's a
	89:21	long level model. It will basically rate
	89:22	things at a level data and then process through
	89:23	our simulation and, you know, 2000, pass, all
	89:24	the probability and then predict numbers of OAS
	89:25	and then, you know, tell us what the return is,
	90:2	you know, for this, and then, you know, credit
	90:3	enhancement levels and all those kinds of
	90:4	things. We can get all of them from the
	90:5	analysis from the model.
	90:6	BY MR. SACCA:

<b>GSE Use of Models in Pre-Purchase Analysis</b>		
	90:7	Q. And this model you are referring to,
	90:8	is this what you described earlier as the model
	90:9	CJ Zhao finished in 2007?
	90:10	A. Yes.
	90:11	Q. Was there some name you used
	90:12	internally for it?
	90:13	A. At the time, not sure there was a
	90:14	name. It was kind of a new product. I know
	90:15	the -- for now, they call them or before this
	90:16	-- this thing is retired already. ABS
	90:17	analytics at certain time.
	90:18	Q. Apart from yourself, do you know if
	90:19	there were others within Capital Markets
	90:20	Strategy who negotiated with issuers about the
	90:21	structure of bonds?
	90:22	A. Our team, so Francisco maybe,
	90:23	definitely Francisco sometimes get involved
	90:24	when, you know, there are certain things I
	90:25	cannot even explain very clearly to the sell
	91:2	side, but definitely traders for sure.
<b>Cao Tr. at 145:13 -- 146:2</b>	145:13	Q. The next bullet talks about a
	145:14	prototype application built for timely
	145:15	stochastic analysis of holdings.
	145:16	Do you know what application that is
	145:17	referring to?
	145:19	THE WITNESS: That's the CJ's model.
	145:20	BY MR. SACCA:
	145:21	Q. And that model was built when?
	145:22	A. It was in -- she was building in
	145:23	2006.
	145:24	Q. And when did Fannie Mae start using
	145:25	that application?
	146:2	A. Early 2007, I would say.
<b>Cao Tr. at 146:13 -- 147:8</b>	146:13	Q. And, at the top, there is an open
	146:14	position for a vice president of PLS asset
	146:15	management.
	146:16	Was that position ever filled during
	146:17	the time you worked in CMS?
	146:18	A. Yes. David Gussmann.
	146:19	Q. Okay. And when did he take that

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	146:20	job?
	146:21	A. I'm not sure it's the end of 2006 or
	146:22	early 2007.
	146:23	Q. There are, under him, what appear to
	146:24	be two direct reports, CJ Zhao and Kin Chung.
	146:25	CJ Zhao is identified as the director of
	147:2	analytics and modeling, is that what you
	147:3	understood her role to be?
	147:4	A. Yes.
	147:5	Q. And what functions did analytics and
	147:6	modeling serve?
	147:7	A. Build a model to evaluate the risk
	147:8	and returns.
<b>Cao Tr. at 232:2 - - 233:6</b>	232:2	THE WITNESS: Yeah. Like I say in
	232:3	my comment, yeah, I have to -- the other one, I
	232:4	have to look at it. Yeah, there is a super
	232:5	center structure for the Alt-A and option ARM
	232:6	that actually is, you know -- if you look at
	232:7	it, super senior/Mezz structure, that structure
	232:8	is supposed to create additional buffer for
	232:9	the -- you know, the top layer, the most senior
	232:10	bound. So looks like based on the contents of
	232:11	the e-mail and then this documentation, I
	232:12	believe at the time in 2007, we wanted to do
	232:13	more in-depth analysis using, you know, CJ's
	232:14	model because this checklist, as you can see,
	232:15	is one dimension of checking the risk of one
	232:16	that is high. But they could be -- you know,
	232:17	the risk could be outside the other factors in
	232:18	the pool and all the other structure. So it's
	232:19	not connected like what the collateral is
	232:20	doing. I don't know, you know, what the
	232:21	structure is doing. You know, the creditor has
	232:22	risk. Structure could mitigate it, so they are
	232:23	not necessarily connected.
	232:24	So CJ's model is supposed to handle
	232:25	that so we will be migrating to, you know, a
	233:2	more level in-depth analysis. It's probably
	233:3	for this kind of super center structure, which
	233:4	we don't have very good understanding from just
	233:5	the checklist to see what kind of risk we are

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	233:6	exposed to.
<b>Cao Tr. at 240:2 - 243:24</b>	240:2	Q. At some point, Fannie Mae stopped
	240:3	the pre-settlement checklist process in favor
	240:4	of a different kind of analysis; is that
	240:5	correct?
	240:6	A. Yes.
	240:7	Q. And that's what you described as CJ
	240:8	Zhao's model?
	240:9	A. Correct.
	240:10	Q. And describe for me, please, the
	240:11	difference between the two approaches?
	240:13	THE WITNESS: Pre-settlement, you
	240:14	can say that it's just a very simple
	240:15	spreadsheet, one page or two of, you know,
	240:16	checking of the invention at the time, right.
	240:17	CJ's model is a stochastic model and then used
	240:18	on other data as input and then collect the
	240:19	cash flow with deal structure throughout the
	240:20	model. So below that, all the information with
	240:21	all the embedded risk factors requested by the
	240:22	model and fit into the process, generally the
	240:23	cash flow, by doing, you know, simulations
	240:24	based on home price interest rates environment
	240:25	and then generated cash flow based on that and
	241:2	then run through the cash flow, you know,
	241:3	through the INTEX, you know, the structure of
	241:4	the deal and then estimate the credit risks and
	241:5	estimate the loss of the bonds and the price of
	241:6	the bonds based on the -- you know, per model.
	241:7	Q. What is a stochastic model?
	241:9	THE WITNESS: Basically using
	241:10	simulation approach to simulate your
	241:11	different -- the key inputs and then outputs
	241:12	the -- you know, different kind of results. So
	241:13	it's kind of probably realistic -- real.
	241:14	BY MR. SACCA:
	241:15	Q. And did you say inputs into the
	241:16	model included loan level data?
	241:17	A. That's required. Loan level, yes.
	241:18	Q. And the loan level data that Fannie

**GSE Use of Models in Pre-Purchase Analysis**

241:19 Mae put into the model was loan level data  
 241:20 specific to the particular deal you were  
 241:21 modeling?  
 241:22 A. Yes.

241:24 BY MR. SACCA:  
 241:25 Q. And from where did you get the data?

242:2 A. From the issuer, the dealer.  
 242:3 Q. And did that come from the loan tape  
 242:4 or the CDI file or --  
 242:5 A. Low level data is from loan tape.  
 242:6 The structure is from CDI.  
 242:7 Q. And what sort of loan level data  
 242:8 went into the model?

242:10 THE WITNESS: Again, there are a lot  
 242:11 of fields that in the data table -- I think we  
 242:12 went through this this morning, so not remember  
 242:13 every single thing, but, you know, LTV, FICO,  
 242:14 coupon, you know, note rates, specifically, and  
 242:15 then seasoning, how long season, and then  
 242:16 geography. That's, you know, the gist of it.  
 242:17 BY MR. SACCA:  
 242:18 Q. And when you were running the model,  
 242:19 you ran it through various scenarios?  
 242:20 A. Correct, yes.  
 242:21 Q. And in running those various  
 242:22 scenarios, did you ever alter any of the -- the  
 242:23 loan level data that you input to see if that  
 242:24 would make a difference in the outcome?

243:2 THE WITNESS: I don't remember doing  
 243:3 that, no.  
 243:4 BY MR. SACCA:  
 243:5 Q. So you -- you never said let's see  
 243:6 what it looks like if we use a different LTV or  
 243:7 different average FICO score?  
 243:8 A. That's not the common practice in  
 243:9 industry to do analysis.  
 243:10 Q. Why did the CMS group switch from  
 243:11 the pre-settlement checklist model to the CJ  
 243:12 Zhao model?

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	243:13	A. Because then this model give us
	243:14	wholistic view of the risk and return.
	243:15	Q. So you thought it would do a better
	243:16	job of assessing risk?
	243:17	A. Definitely.
	243:18	Q. Did you perceive that the
	243:19	pre-settlement checklist process didn't
	243:20	accurately capture risk?
	243:22	THE WITNESS: It's -- I wouldn't say
	243:23	it's not accurate. It's just limited compared
	243:24	to this more extensive model.
<b>Cao Tr. at 689:4 - 690:12</b>	689:4	Q. For the most part, when these loans
	689:5	were originated, it was the originators that
	689:6	was responsible for originating them in
	689:7	accordance with the guidelines that Fannie Mae
	689:8	set, correct?
	689:10	THE WITNESS: I believe so.
	689:11	BY MR. HARSCH:
	689:12	Q. So now in the models that you ran to
	689:13	determine the intrinsic value of these
	689:14	mortgages, did Fannie Mae incorporate any
	689:15	variables that reflected the degree to which
	689:16	Fannie Mae felt that these originators had
	689:17	adhered to the guidelines to which these loans
	689:18	were supposed to have been originated?
	689:20	THE WITNESS: Not we ran
	689:21	underwriting it? We underwrite it or -- we do
	689:22	have called, you know, getting to the model
	689:23	components, we have an ACI model which is kind
	689:24	of super-FICO kind of index we created, based
	689:25	on the borrower information that actually have
	690:2	all this borrower-specific information, FICOs,
	690:3	and all that information, income, TDI, LTV, all
	690:4	fits into it, and then we would come out with,
	690:5	like, we call them super-FICO. So it's helped
	690:6	to identify the risk of the borrowers, so we
	690:7	never really -- I mean, under -- we ran -- the
	690:8	underwriting was not in the model, right.
	690:9	BY MR. HARSCH:

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	690:10	Q. The underwriting was not in the
	690:11	model?
	690:12	A. No.



<b>Policies for Purchasing PLS and Selecting Collateral Backing PLS</b>	
<b>D. Cook Tr. at 385:23 -- 387:2</b>	<p>385:23 Q The subject is "New process for submitting 385:24 loan tapes." It's from Shayan Salahuddin to Joe Haley 385:25 and Richard Perrelli, dated February 2 -- 22, 2007.</p> <p>386:3 Is it correct that this document reflects a 386:4 process for "collateral selection in PLS 386:5 transactions"?</p> <p>386:6 A Yes.</p> <p>386:7 Q What is meant by "collateral selection"?</p> <p>386:8 A When the dealers were putting together a 386:9 deal, a PLS, depending on which collateral would be 386:10 included in the deal, it could yield higher goals 386:11 score value for housing goals purposes for Fannie Mae, 386:12 all else equal.</p> <p>386:13 Q What is the "selection" in "collateral 386:14 selection"?</p> <p>386:16 A Selecting which loans to include in the deal 386:17 that Fannie Mae purchases.</p> <p>386:18 Q Fannie Mae participated in that collateral 386:19 selection process in order to determine which loans to 386:20 include in the deal for housing goal purposes, 386:21 correct?</p> <p>386:23 A Yes.</p> <p>386:24 Q That was Fannie Mae's practice, correct?</p> <p>387:2 A Yes.</p>
<b>D. Cook Tr. at 387:8 -- 12</b>	<p>387:8 Q There were procedures written about Fannie 387:9 Mae's participation in the collateral selection 387:10 process for housing goal purposes, correct?</p> <p>387:12 A Yes</p>
<b>D. Cook Tr. at 391:15 -- 392:7</b>	<p>391:15 Q Did Fannie Mae have a practice of 391:16 participating in collateral selection for PLS 391:17 purchases during 2005 to 2007 other than the 391:18 collateral selection we've been discussing for 391:19 purposes of pursuing housing goals?</p> <p>391:21 A Yes.</p> <p>391:22 Q Can you describe what that collateral 391:23 selection consisted of at Fannie Mae in that period?</p>

	<p>391:25 A The traders, Ashley Dyson and Steve Shen,</p> <p>392:2 told me that they would also opine -- rather,</p> <p>392:3 separately, for purposes of housing goals, they would</p> <p>392:4 ask for the collateral characteristics to be a certain</p> <p>392:5 way, and they would work with the dealers to try to</p> <p>392:6 meet their preferred collateral composition for a risk</p> <p>392:7 and return standpoint.</p>
<b>D. Cook Tr. at 392:15 -- 393:15</b>	<p>392:15 Q Did anyone else participate with the traders</p> <p>392:16 in collateral selection other than Housing Goals</p> <p>392:17 people?</p> <p>392:19 A Yes.</p> <p>392:20 Q Who else?</p> <p>392:21 A The Capital Markets Strategy or Capital</p> <p>392:22 Markets Risk team at some point during that period</p> <p>392:23 also started to assist the traders in providing a</p> <p>392:24 preferred collateral composition.</p> <p>392:25 Q Do you know at what point that began?</p> <p>393:2 A I believe it began during the 2006 year.</p> <p>393:3 And I believe in the policy that was drafted in 2007,</p> <p>393:4 it may refer to their role to do prepurchase reviews.</p> <p>393:5 Q So in -- starting in 2006 and carrying into</p> <p>393:6 2007, personnel from Capital Markets Strategy or the</p> <p>393:7 Risk team participated with the traders in collateral</p> <p>393:8 selection in PLS, correct?</p> <p>393:10 A They did participate in reviewing the</p> <p>393:11 collateral. Depends on what you mean by collateral</p> <p>393:12 selection. I think the selection of loans to include</p> <p>393:13 and exclude was primarily the responsibility of the</p> <p>393:14 traders, but they had assistance from the Risk team</p> <p>393:15 and the Housing Goals Scoring team.</p>
<b>Palmer Tr. at 642:9 -- 642:23</b>	<p>642:9 Q. Okay, great. I take it from</p> <p>642:10 your testimony yesterday that you weren't</p> <p>642:11 involved in the selection of loans that</p> <p>642:12 went into the supporting loan groups for</p> <p>642:13 PLS that Freddie purchased; is that</p> <p>642:14 right?</p> <p>642:15 A. That's correct.</p> <p>642:16 Q. But were you aware that during</p> <p>642:17 the 2005 to 2007 time period that there</p> <p>642:18 were other people at Freddie Mac that</p> <p>642:19 were involved in either removing or</p>

	<p>642:20 adding loans into the pools for housing</p> <p>642:21 goals purposes?</p> <p>642:23 A. I was aware.</p>
<b>Wood Tr. at 234:17 -- 235:17</b>	<p>234:17 Q. Do you see the title of the</p> <p>234:18 attachment is: "Credit risk oversight mortgage</p> <p>234:19 ABS summary?"</p> <p>234:20 A. Yes.</p> <p>234:21 Q. And if you go to the bottom of that</p> <p>234:22 page, do you see a bullet that says: "Mortgage</p> <p>234:23 ABS buy strategy," it's bolded?</p> <p>234:24 A. Yes.</p> <p>234:25 Q. And then below that, it states:</p> <p>235:2 "Currently, only Triple A investments</p> <p>235:3 considered. Two main drivers, growth and</p> <p>235:4 affordable housing goals. Purchases must meet</p> <p>235:5 ROE threshold of 9 percent. Majority of</p> <p>235:6 purchases are over 20 percent ROE. Deploy</p> <p>235:7 capital. Emphasis being placed on purchases</p> <p>235:8 aimed to help meet 2005 HUD affordable housing</p> <p>235:9 goals which have not been clearly defined to</p> <p>235:10 date. 25 percent of the portfolio manager's</p> <p>235:11 time is being dedicated to purchases that help</p> <p>235:12 meet HUD goals."</p> <p>235:13 Do you see that?</p> <p>235:14 A. Uh-huh.</p> <p>235:15 Q. What is ROE as used in this set of</p> <p>235:16 bullets?</p> <p>235:17 A. Return on equity.</p>
<b>Kenneweg 30(b)(6) Tr. at 71:22 -- 72:7</b>	<p>71:22 Q. Yes. Did Freddie Mac have any</p> <p>71:23 policy or procedure that would have prevented</p> <p>71:24 it from purchasing PLS backed by loans from</p> <p>71:25 originators whose guidelines made exceptions</p> <p>72:2 largely unnecessary?</p> <p>72:5 A. I've never -- I've never seen</p> <p>72:6 that wording in a policy or procedure, that</p> <p>72:7 would prevent that type of purchase.</p>
<b>Kenneweg 30(b)(6) Tr. at 73:2 -- 73:12</b>	<p>73:2 Q. Common sense underwriting</p> <p>73:3 decisions. Did Freddie Mac have any policy or</p> <p>73:4 procedure that prevented it from purchasing</p> <p>73:5 PLS backed by loans from originators whose</p> <p>73:6 files did not evidence common sense</p> <p>73:7 decision-making?</p>

	<p>73:10 A. I haven't seen explicitly  73:11 common sense referred to in our policies or  73:12 procedures.</p>
<p><b>Kenneweg  30(b)(6) Tr. at  82:14 – 85:4</b></p>	<p>82:14 Q. So under Freddie Mac's policies  82:15 and procedures, would these comments and  82:16 observations merit a rating of poor with  82:17 respect to credit?  82:20 A. I don't know the specific  82:21 criteria that would cause a particular rating  82:22 on a subcategory. I don't know.  82:23 Q. Would comments like this under  82:24 Freddie's policies and procedures result in a  82:25 suspension of purchasing PLS backed by ResMAE    83:2 loans?    83:5 A. Freddie Mac's purchase of PLS  83:6 securities would be governed by policies and  83:7 procedures that don't reference this level of  83:8 granular comments.  83:9 Q. Right. But you are familiar  83:10 with policies and procedures. Right?    83:13 A. I am.  83:14 Q. You've been working with them  83:15 for a number of years now. Right?    83:18 A. Not all policies and  83:19 procedures, but yes.  83:20 Q. Right. The ones with respect  83:21 to the decision-making behind PLS. Right?    83:24 A. Yes.  83:25 Q. And you were familiar with the    84:2 ones that were in effect in 2006 and 2007.  84:3 Right?    84:6 A. Yes.  84:7 Q. And based on your knowledge of  84:8 those procedures, would they have required  84:9 that Freddie Mac suspend purchases of PLS  84:10 backed by ResMAE loans in light of the  84:11 comments here?</p>

	<p>84:14 A. No.</p> <p>84:15 Q. Did Freddie Mac also review --</p> <p>84:16 MR. SECHLER: Strike that.</p> <p>84:17 BY MR. SECHLER:</p> <p>84:18 Q. Did AMO also perform</p> <p>84:19 operational reviews of issuers and</p> <p>84:20 aggregators?</p> <p>84:21 A. Yes.</p> <p>84:22 Q. What types of information did</p> <p>84:23 AMO consider in those operational reviews?</p> <p>84:24 A. Due diligence processes.</p> <p>84:25 Overall controls. So a lot of the categories</p> <p>85:2 would be similar to an originator review,</p> <p>85:3 except there wouldn't be the credit, like</p> <p>85:4 underwriting-type consideration.</p>
<p><b>Kenneweg</b>  <b>30(b)(6) Tr. at</b>  <b>87:19 – 88:10</b></p>	<p>87:19 Q. And what rate was given --</p> <p>87:20 A. Reviews.</p> <p>87:21 Q. -- to AMO written reviews in</p> <p>87:22 the assessment of PLS counterparties?</p> <p>87:24 A. I don't -- it wasn't an</p> <p>87:25 explicit weight.</p> <p>88:2 Q. Was it a significant factor?</p> <p>88:5 A. It was. It could be.</p> <p>88:6 Q. Was it more significant in the</p> <p>88:7 process than external ratings?</p> <p>88:8 A. I think that probably depends</p> <p>88:9 on the type of review that was being</p> <p>88:10 completed.</p>
<p><b>Kenneweg</b>  <b>30(b)(6) Tr. at</b>  <b>88:17 – 90:22</b></p>	<p>88:17 Q. Sure. These AMO written</p> <p>88:18 reviews, they were used to determine whether</p> <p>88:19 or not to approve a PLS counterparty?</p> <p>88:22 A. That wasn't the sole use, but</p> <p>88:23 it was a consideration.</p> <p>88:24 Q. Well, that was a use?</p> <p>88:25 A. Right. Right.</p> <p>89:2 Q. They were also used to develop</p> <p>89:3 a metric score for PLS counterparties. Right?</p> <p>89:4 A. Correct.</p> <p>89:5 Q. And they were used in</p> <p>89:6 connection with the ongoing monitoring of PLS</p>

	<p>89:7 counterparties. Correct?</p> <p>89:10 A. Yes.</p> <p>89:11 Q. Now, which counterparties in</p> <p>89:12 the PLS business --</p> <p>89:13 MR. SECHLER: That's terrible.</p> <p>89:14 Strike that.</p> <p>89:15 BY MR. SECHLER:</p> <p>89:16 Q. Which PLS counterparties</p> <p>89:17 required approval by counterparty credit risk</p> <p>89:18 management?</p> <p>89:19 A. There is a chart within the</p> <p>89:20 procedure. So if you go to the procedure,</p> <p>89:21 Appendix A.</p> <p>89:22 Q. Yes.</p> <p>89:23 A. Servicers and originators, once</p> <p>89:24 they -- once they -- once we accumulated above</p> <p>89:25 one percent of the portfolio, in terms of UPB,</p> <p>90:2 with that counterparty, and then issuers would</p> <p>90:3 be at time of first trade, they would require</p> <p>90:4 approval.</p> <p>90:5 Q. And is that --</p> <p>90:6 MR. SECHLER: Strike that.</p> <p>90:7 BY MR. SECHLER:</p> <p>90:8 Q. Was that the practice</p> <p>90:9 throughout the period from when you started in</p> <p>90:10 counterparty credit risk management through</p> <p>90:11 the end of 2007?</p> <p>90:12 A. I believe so. And I should --</p> <p>90:13 you know what; can I clarify my statement?</p> <p>90:14 Q. Sure.</p> <p>90:15 A. I just said issuers require</p> <p>90:16 approval at first trade. It's caveated based</p> <p>90:17 on the status of the originators within the</p> <p>90:18 deal.</p> <p>90:19 Q. So if originators in the deal</p> <p>90:20 were all rated between M-1 and M-5, an issuer</p> <p>90:21 would not require counterparty approval?</p> <p>90:22 A. Right.</p>
<p><b>Kenneweg</b></p> <p><b>30(b)(6) Tr. at</b></p> <p><b>71:22 -- 72:7</b></p>	<p>71:22 Q. Yes. Did Freddie Mac have any</p> <p>71:23 policy or procedure that would have prevented</p> <p>71:24 it from purchasing PLS backed by loans from</p> <p>71:25 originators whose guidelines made exceptions</p> <p>72:2 largely unnecessary?</p>

	<p>72:5 A. I've never -- I've never seen</p> <p>72:6 that wording in a policy or procedure, that</p> <p>72:7 would prevent that type of purchase.</p>
<p><b>Kenneweg</b></p> <p><b>30(b)(6) Tr. at</b></p> <p><b>73:2 -- 12</b></p>	<p>73:2 Q. Common sense underwriting</p> <p>73:3 decisions. Did Freddie Mac have any policy or</p> <p>73:4 procedure that prevented it from purchasing</p> <p>73:5 PLS backed by loans from originators whose</p> <p>73:6 files did not evidence common sense</p> <p>73:7 decision-making?</p> <p>73:10 A. I haven't seen explicitly</p> <p>73:11 common sense referred to in our policies or</p> <p>73:12 procedures.</p>
<p><b>Syron Tr. at</b></p> <p><b>129:14 -- 130:12</b></p>	<p>129:14 Q. And it says here, "As long as</p> <p>129:15 some institutions operate under</p> <p>129:16 different, or no, regulatory strictures,</p> <p>129:17 potential for these sorts of excesses and</p> <p>129:18 abuses will exist. As previously stated,</p> <p>129:19 Freddie Mac has a long history of</p> <p>129:20 voluntarily setting standards of prudent</p> <p>129:21 underwriting and of promoting greater</p> <p>129:22 borrower protections in subprime."</p> <p>129:23 Do you see that?</p> <p>129:24 A. Yes.</p> <p>129:25 Q. And was that a true statement?</p> <p>130:1</p> <p>130:2 A. Yes.</p> <p>130:3 Q. When you referred to prudent</p> <p>130:4 underwriting, can you describe what you</p> <p>130:5 meant there?</p> <p>130:6 A. Prudent underwriting would</p> <p>130:7 mean that it was not predatory.</p> <p>130:8 Q. What do you mean by not</p> <p>130:9 predatory?</p> <p>130:10 A. That in fact we expected the</p> <p>130:11 person who took the loan would be able to</p> <p>130:12 service it.</p>

Use of Credit Enhancement in PLS	
<b>Bisenius Tr. at 155:25 -- 156:8</b>	<p>155:25 Q In the PLS business, would a credit</p> <p>156:2 enhancement include if you were buying, for example,</p> <p>156:3 the AAA tranche, the portion of those losses that</p> <p>156:4 would be absorbed by lower tranches in the PLS</p> <p>156:5 securitization?</p> <p>156:7 A I would include that as, in my thoughts, a</p> <p>156:8 definition of what a credit enhancement is, yes.</p>
<b>Bisenius Tr. at 288:1 -- 290:15</b>	<p>288:2 Q So having read the memo, does that refresh</p> <p>288:3 your recollection about the process that was being</p> <p>288:4 attempted to be used to use DEFCAP to help to value</p> <p>288:5 the credit underlying MABS portfolio purposes?</p> <p>288:7 A As I look at this, I recall there being</p> <p>288:8 conversations around doing this one, yes.</p> <p>288:9 Q Great.</p> <p>288:10 Maybe let's just start with, what do you</p> <p>288:11 recall about the conversations?</p> <p>288:12 A Pretty much what's summarized in the memo</p> <p>288:13 itself, which was recognizing that DEFCAP was not</p> <p>288:14 designed for pools, it was designed for loan-level</p> <p>288:15 type analysis, was there a way that we could use</p> <p>288:16 pool-type stratifications and still capture them</p> <p>288:17 within DEFCAP. I also recall there being a discussion</p> <p>288:18 about kind of a level of information that Freddie Mac</p> <p>288:19 received prior to its purchase of private label</p> <p>288:20 securities and whether that information needed to be</p> <p>288:21 expanded to be able to allow them to use the DEFCAP</p> <p>288:22 type model.</p> <p>288:23 Q So you recall that there was a proposal to</p> <p>288:24 require dealers to provide breakdowns of their pool by</p> <p>288:25 FICO/LTV buckets?</p> <p>289:2 A That's -- as this thing suggests, that's my</p> <p>289:3 recollection.</p> <p>289:4 Q And then there would also be 12 FICO/LTV</p> <p>289:5 grids which would be used to evaluate those pools; is</p> <p>289:6 that correct?</p> <p>289:8 A Again, as the memo describes, I didn't</p> <p>289:9 recall the 12, but it says 12, that makes sense.</p>



Use of Credit Enhancement in PLS	
	<p>289:10 Q Right.</p> <p>289:11 Do you recall then that those grids would be</p> <p>289:12 populated in terms of expected loss by running the</p> <p>289:13 DEFCAP model?</p> <p>289:15 A Again, that's my general recollection having</p> <p>289:16 read this. That's right.</p> <p>289:17 Q And do you recall that they would run the</p> <p>289:18 DEFCAP model at different levels, at the 50 percent,</p> <p>289:19 the 99 percent, the 100 percent, to see what losses</p> <p>289:20 would be projected under each of the different</p> <p>289:21 scenarios under DEFCAP?</p> <p>289:23 A I don't recall that specifically. I know</p> <p>289:24 there was some desire -- because, again, we're talking</p> <p>289:25 about the investment in the retained portfolio. It's</p> <p>290:2 not as much about the loan level as it is about the</p> <p>290:3 subordination level and the, kind of, risk of the</p> <p>290:4 structure. I think that's what they were trying to do</p> <p>290:5 for the risk of the structure, but I don't have as</p> <p>290:6 clear of a recollection on that.</p> <p>290:7 Q Right. And so, generally, do you understand</p> <p>290:8 the idea was to estimate the risk of potential losses</p> <p>290:9 using the DEFCAP model and then figure out whether the</p> <p>290:10 credit enhancements that were provided in the security</p> <p>290:11 structure would be sufficient to protect against that</p> <p>290:12 level of losses?</p> <p>290:14 A That's my understanding of what they were</p> <p>290:15 trying to do, that's right</p>
<b>Bisenius Tr. at 559:11 -- 559:22</b>	<p>559:11 Q We saw some documents yesterday referring to</p> <p>559:12 investing in AAA tranches of PLS to get protection</p> <p>559:13 from the credit enhancement that that afforded. Do</p> <p>559:14 you remember that?</p> <p>559:16 A Protection from the credit risk.</p> <p>559:17 Q I should say by the credit enhancement from</p> <p>559:18 the credit risk.</p> <p>559:19 A I recall looking at those documents, yes.</p> <p>559:20 Q Is that generally consistent with your</p> <p>559:21 recollection of Freddie Mac's policy regarding</p> <p>559:22 investment in PLS?</p>

**Use of Credit Enhancement in PLS**

**Aneiro Tr. at  
274:5 -- 275:23**

274:5 Q. Now, how was the DEFCAP, how  
274:6 were the DEFCAP results used for the  
274:7 credit analysis?

274:8 A. I don't remember specifically,  
274:9 but in general it defined what the  
274:10 various percentiles of the -- of the  
274:11 various paths were in terms of the  
274:12 quantifying total losses in the various  
274:13 percentiles and then compared to what the  
274:14 subordination level was underneath the  
274:15 tranche that we were buying.

274:16 Q. And when you said the  
274:17 subordination level, you mean the credit  
274:18 enhancement provided?

274:19 A. Yes.

274:20 Q. And if the credit enhancement  
274:21 provided was greater than the -- well,  
274:22 was there a need to compare the -- you  
274:23 said there was a comparison of the credit  
274:24 enhancement provided to the DEFCAP  
274:25 results. What happened if the credit  
275:1 enhancement provided was greater than the  
275:2 expected losses calculated by DEFCAP?

275:3 A. That would be a positive.

275:4 Q. What do you mean by positive?

275:5 A. That means that we would have  
275:6 more protection than what the various  
275:7 percentiles of results of the DEFCAP  
275:8 model predicted as losses. So we would  
275:9 have more protection than the expected  
275:10 losses defined by DEFCAP.

275:11 Q. How would that impact the  
275:12 credit analysis of the deal?

275:13 A. That would be a positive in  
275:14 approving the credit analysis.

275:15 Q. So the credit analysis would  
275:16 be approved if the credit enhancement was  
275:17 greater than the DEFCAP 100th percentile,  
275:18 correct?

275:19 A. I don't know if it's a hundred  
275:20 percentile, I don't recall the policy.

275:21 It's not the only -- only thing that  
275:22 would be evaluated, but it would be a

Use of Credit Enhancement in PLS	
	275:23 positive in the evaluation of a deal.
<b>Aneiro Tr. at 280:22 -- 281:9</b>	<p>280:22 Q. So that makes sense. So then</p> <p>280:23 if this statement is correct, if the</p> <p>280:24 credit enhancement for a deal is greater</p> <p>280:25 than the expected loss calculated by</p> <p>281:1 DEFCAP, the credit enhancement for the</p> <p>281:2 deal can be approved; is that correct?</p> <p>281:3 A. That's my understanding of</p> <p>281:4 this.</p> <p>281:5 Q. And in order to obtain credit</p> <p>281:6 approval, however, you would still need</p> <p>281:7 the counterparty approval?</p> <p>281:8 A. That's what -- that's how I</p> <p>281:9 recall the practice to be.</p>
<b>Kain Tr. at 272:9 -- 275:13</b>	<p>272:9 Q. Do you recognize 20418 as a trade</p> <p>272:10 ticket for a transaction CWL 05 -- 2005 -- 4:</p> <p>272:11 2AV1?</p> <p>272:13 THE WITNESS: Yes, I do.</p>
<b>Kain Tr. at 272:22 -- 273:14</b>	<p>272:22 Q. If you flip into the package a</p> <p>272:23 little bit, to the page with the Bates number</p> <p>272:24 ending in 924, there are a couple of e-mails</p> <p>272:25 here.</p> <p>273:2 The bottom e-mail is a credit</p> <p>273:3 approval from Scott Devine. Do you remember</p> <p>273:4 Mr. Devine?</p> <p>273:5 A. I remember him vaguely, yes.</p> <p>273:6 Q. Do you remember what organization he</p> <p>273:7 worked in?</p> <p>273:8 A. I don't at that time.</p> <p>273:9 Q. And then he writes: "Credit</p> <p>273:10 approved," and way at the bottom: "Credit</p> <p>273:11 enhancement is adequate relative to expected</p> <p>273:12 losses."</p> <p>273:13 Do you see that?</p> <p>273:14 A. I see that.</p>
<b>Kain Tr. at 273:20 -- 275:13</b>	<p>273:20 Q. And was that determination: "The</p> <p>273:21 credit enhancement is adequate relative to</p> <p>273:22 expected losses," is that the credit approval</p> <p>273:23 for this transaction?</p> <p>273:25 THE WITNESS: I am not sure.</p>

**Use of Credit Enhancement in PLS**

	<p>274:2 BY MR. BENNETT:</p> <p>274:3 Q. If you look above that, there is an</p> <p>274:4 e-mail from Frank Vetrano to Scott Devine that</p> <p>274:5 says: "Approved," and then below that:</p> <p>274:6 "Scott, is 30 percent credit enhancement or CE</p> <p>274:7 here a record for us. Please highlight the</p> <p>274:8 risk characteristics that scared the rating</p> <p>274:9 agencies."</p> <p>274:10 Do you see that?</p> <p>274:11 A. I see that, yeah.</p> <p>274:12 Q. Do you understand what Mr. Vetrano</p> <p>274:13 meant by that?</p> <p>274:14 A. I have no record of this e-mail from</p> <p>274:15 my memory, but there was -- it appears that</p> <p>274:16 this deal required 30 percent credit</p> <p>274:17 enhancement, and so Frank wanted -- seems to be</p> <p>274:18 asking the question, why was the credit</p> <p>274:19 enhancement required. That was required that</p> <p>274:20 high. I mean, that's my interpretation but I</p> <p>274:21 am looking at it like you are.</p> <p>274:22 Q. And the credit enhancement is</p> <p>274:23 something that was set by the rating agencies</p> <p>274:24 to provide protection to the Triple A tranche?</p> <p>274:25 A. Yes, generally, but there are times</p> <p>275:2 when we have asked for more credit enhancement</p> <p>275:3 on our own, I believe, so -- but in this case,</p> <p>275:4 it appears that Frank at least believed that</p> <p>275:5 the rating agencies were responsible for the</p> <p>275:6 higher credit enhancement.</p> <p>275:7 Q. And as you pointed out, sometimes</p> <p>275:8 Freddie Mac's own assessment was that the deal</p> <p>275:9 was riskier than the rating agencies thought,</p> <p>275:10 so Freddie asked for more enhancement, didn't</p> <p>275:11 they?</p> <p>275:12 A. I believe there were cases like</p> <p>275:13 that, yes.</p>
<p><b>Cao Tr. at 87:16 - 89:9</b></p>	<p>87:16 What were Fannie Mae's investment</p> <p>87:17 interests?</p> <p>87:19 THE WITNESS: The credit enhancement</p> <p>87:20 levels we want to have to mitigate the risk and</p> <p>87:21 then the yield we want.</p>

Use of Credit Enhancement in PLS		
	87:22	BY MR. SACCA:
	87:23	Q. What is credit enhancement?
	87:24	A. It's the credit enhancement for --
	87:25	in the structure, that -- you have a structure,
	88:2	right, so the bonds you buy, anything below it,
	88:3	it was supposed to take first loss and those
	88:4	collaterals or those files are supposed to be
	88:5	your credit enhancements, that's one type of
	88:6	them, and you could have third-party insurance.
	88:7	They could go out and get a wrap, which is
	88:8	called wrap, and then so basically, have
	88:9	insurance company guarantee that this bond is
	88:10	not going to take a loss.
	88:11	That is additionally enhancement,
	88:12	and then there is other things like you could
	88:13	have a reserve fund account set up that
	88:14	actually has additional monies set aside, that
	88:15	is another credit enhancement.
	88:16	Q. And you said another part of the
	88:17	discussions you could have or -- sorry, another
	88:18	one of Fannie Mae's investment interest was the
	88:19	yield you wanted. That's the return to Fannie
	88:20	Mae on the bond?
	88:21	A. Yes.
	88:22	Q. And that was something that Fannie
	88:23	Mae could and did negotiate with issuers of
	88:24	bonds?
	88:25	A. Definitely.
	89:2	Q. And credit enhancement was something
	89:3	Fannie Mae found it could and did negotiate
	89:4	with issuers of bonds?
	89:5	A. Yes.
	89:6	Q. And there were times when you were
	89:7	successful in getting issuers of bonds to
	89:8	change the structure to meet your requirements?
	89:9	A. Yes.
<b>Cao Tr. at 90:2 - 91:2</b>	90:2	you know, for this, and then, you know, credit
	90:3	enhancement levels and all those kinds of
	90:4	things. We can get all of them from the
	90:5	analysis from the model.

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	<p>90:7 Q. And this model you are referring to,</p> <p>90:8 is this what you described earlier as the model</p> <p>90:9 CJ Zhao finished in 2007?</p> <p>90:10 A. Yes.</p> <p>90:11 Q. Was there some name you used</p> <p>90:12 internally for it?</p> <p>90:13 A. At the time, not sure there was a</p> <p>90:14 name. It was kind of a new product. I know</p> <p>90:15 the -- for now, they call them or before this</p> <p>90:16 -- this thing is retired already. ABS</p> <p>90:17 analytics at certain time.</p> <p>90:18 Q. Apart from yourself, do you know if</p> <p>90:19 there were others within Capital Markets</p> <p>90:20 Strategy who negotiated with issuers about the</p> <p>90:21 structure of bonds?</p> <p>90:22 A. Our team, so Francisco maybe,</p> <p>90:23 definitely Francisco sometimes get involved</p> <p>90:24 when, you know, there are certain things I</p> <p>90:25 cannot even explain very clearly to the sell</p> <p>91:2 side, but definitely traders for sure.</p>
<b>Cao Tr. at 183:22 - 184:21</b>	<p>183:22 Q. Did you have any understanding of</p> <p>183:23 the rationale for any of the tests on the</p> <p>183:24 checklist?</p> <p>184:2 THE WITNESS: I totally understand</p> <p>184:3 they are credit policy, credit risk-related</p> <p>184:4 issues, that we want to safeguard and -- yeah.</p> <p>184:5 BY MR. SACCA:</p> <p>184:6 Q. For example, the one I just read to</p> <p>184:7 you about the difference in sizing levels, what</p> <p>184:8 was your understanding of why that was</p> <p>184:9 significant?</p> <p>184:10 A. You mean credit enhancement levels</p> <p>184:11 or -- the DOW credit enhancement levels. The</p> <p>184:12 first item?</p> <p>184:13 Q. Yes.</p> <p>184:14 A. This first item is talking about the</p> <p>184:15 difference of setting levels among all the</p> <p>184:16 rating agencies that we get rating from, so we</p> <p>184:17 don't want to see different opinion from</p> <p>184:18 different rating agencies so that indicates,</p> <p>184:19 you know, they observe different kind of risk</p> <p>184:20 embedded in the collateral, so that is what the</p>

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	184:21	language is.
<b>Cao Tr. at 185:19 -- 24</b>	185:19 185:20 185:21 185:22 185:23 185:24	Q. Under Structure Analysis No. 4 is: "CE percent," and then in parentheses, "(subordination and over-collateralization) is greater than or equal to 15 percent." CE percent is credit enhancement? A. Yes.
<b>Cao Tr. at 186:8-14</b>	186:8 186:9 186:10 186:11 186:12 186:13 186:14	Q. Do you know the rationale for the 15 percent? A. I -- actually, I don't know. I can, you know, I don't want to speculate, but it's must be the minimum required, you know, mitigation for the risk for this kind of security. This is for subprime.
<b>Cao Tr. at 208:19 -- 210:7</b>	208:19 208:20 208:21 208:22 208:23 208:24 208:25  209:2 209:3 209:4 209:5 209:6 209:7 209:8 209:9 209:10 209:11 209:12 209:13 209:14 209:15 209:16 209:17 209:18 209:19 209:20 209:21 209:22	Q. Let me show you a document that has been marked as Exhibit 4408. The first page is an e-mail from you to Kin Chung? A. Yes. Q. Saying: "I've completed the pre-settlement review for ABFC 2006-OPT3A1.  This bond is put on conditional retain due to 100 percent of collateral is with CLTV greater than 80 percent." And the next sentence says: "It seems bankers are making mistakes of inputting CE percent as sizing level." Do you see that? A. Yes. Q. Is that last sentence related in any way to the sentence before it? A. Oh, definitely. Q. And can you explain that to me? A. Basically I observed really high risk in the collateral, and I anticipate higher credit enhancement with larger bond. Obviously, the sizing level is far below than what I wanted to see on the credit enhancement level. That is what I was trying to say, you know. Could be a mistake because. Q. So this -- you perceived to be a very risky bond?

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	209:23	A. Well, yes.
	209:24	Q. Okay.
	209:25	A. Just basically, it is a mitigation
	210:2	of the risk. And the reason we're buying
	210:3	Triple A is because we trying to mitigate a
	210:4	risk in the collateral. So when you see
	210:5	collateral so risky, you anticipate seeing
	210:6	higher credit enhancements which I am not
	210:7	seeing in the mitigation of the risk.
<b>Cao Tr. at 217:13 - 218:15</b>	217:13	Q. And what do you consider very good
	217:14	credit enhancement?
	217:17	THE WITNESS: Sufficient to protect
	217:18	the Triple A bonds that we actually were in.
	217:19	BY MR. SACCA:
	217:20	Q. And what would that be in this
	217:21	context?
	217:23	THE WITNESS: So basically, like, I
	217:24	do analysis, I would do Intex or in our model
	217:25	to see anything break it, you know, just trying
	218:2	the different things that we try to break the
	218:3	bond and see if this is the conundrum that
	218:4	actually breaks that bond. And then whether
	218:5	that is easy enough, right?
	218:6	BY MR. SACCA:
	218:7	Q. By the time you had been through
	218:8	your pre-settlement review to make a
	218:9	recommendation on retain or conditional retain,
	218:10	you knew what the credit enhancement on the
	218:11	bond was, correct?
	218:12	A. I should have that information, yes.
	218:13	Q. Right. That's an element of the
	218:14	pre-settlement review?
	218:15	A. Yes. It's in the checklist.
<b>Dyson Tr. at 471:23 – 473:5</b>	471:23	Q. But one of the reasons why credit
	471:24	for a low-doc and no-doc loans is riskier than
	471:25	full-doc loans is because you don't have the
	472:2	borrower's substantiation, right?



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	<p>472:4 THE WITNESS: Yes. That's usually  472:5 reflected in the higher rate that they pay when  472:6 they obtain their loan.</p> <p>472:7 BY MR. BREBNER:</p> <p>472:8 Q. And that is then -- that higher rate  472:9 is then passed on in the PLS pools of those  472:10 loans that Fannie purchases or purchased,  472:11 correct?</p> <p>472:12 A. Yes, for every loan that Fannie  472:13 purchases, that's passed on.</p> <p>472:14 Q. So when Fannie purchased pools of  472:15 subprime loans, there was collateral in the  472:16 pool and there was subordination and  472:17 overcollateralization, Fannie Mae as a  472:18 sophisticated player in the mortgage industry  472:19 fully understood that there were going to be  472:20 loans within those pools that would default,  472:21 correct?</p> <p>472:23 THE WITNESS: Of -- of course that  472:24 is always a possibility. That's why credit  472:25 enhancement exists on the loans that we</p> <p>473:2 purchase is because those tranches are meant to  473:3 absorb any losses as a result of those defaults  473:4 and cushion our bonds from -- from taking  473:5 losses.</p>
<b>Gussman Tr. at 124:23 -- 127:5</b>	<p>124:23 Q. In general, did you have an  124:24 understanding in 2007 about the rating  124:25 agency methodologies with respect to PLS?</p> <p>125:3 A. Yes.</p> <p>125:4 Q. And what was that general  125:5 understanding?</p> <p>125:6 A. So it varied across rating  125:7 agency, but generally, they would size  125:8 bonds so that under different  125:9 hypothetical bad HPA -- sorry, bad house  125:10 price scenarios, different bonds would  125:11 take losses and other bonds wouldn't take  125:12 losses. So, for instance, I forgot which  125:13 historical scenario most of them pointed  125:14 to, but like if you had a huge housing</p>

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	<p>125:15 crash and housing prices went down a  125:16 bunch, the AAA bonds were supposed to  125:17 survive but subordinate bonds would get  125:18 wiped out. They all had sort of  125:19 different nuances.</p> <p>125:20 Q. When you say they sized bonds,  125:21 are you referring to the credit  125:22 enhancement that was built into the  125:23 bonds?</p> <p>125:24 A. Sorry, yes, I'm referring to  125:25 the credit enhancement that's built into</p> <p>126:2 the bonds.</p> <p>126:3 Q. And what form did the credit  126:4 enhancement built into the bonds take?</p> <p>126:6 A. The credit enhancement to the  126:7 bonds would be different for different,  126:8 different types of securities. So the  126:9 most basic is just where you have  126:10 subordinate bonds that take losses first.  126:11 Other bonds could have  126:12 over-collateralization, and this means  126:13 that there could be more loans than  126:14 bonds, so some of the loans could take  126:15 losses before the bonds would take  126:16 losses. There was also another form of  126:17 credit enhancement which is called XS  126:18 spread. So if the coupon on the  126:19 securitization was one, for instance, and  126:20 the coupon on the loans was three, there  126:21 would be an extra 2 percent, and I'm  126:22 generalizing here, making simple. But  126:23 there would be an extra 2 percent in  126:24 interest that would go -- that could be  126:25 used to absorb losses. And then the</p> <p>127:2 final form -- the final form of sort of  127:3 major credit enhancement could be if  127:4 there was a guarantee on the bond from a  127:5 financial guarantor.</p>
Niculescu Tr. at 40:14 to 41:9	<p>40:14 Q. Okay. During the course of the  40:15 day I am going to be asking you questions and</p>

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40:16 all of my questions, unless I otherwise  
40:17 indicate, will be directed to the 2005 to 2007  
40:18 time period. Okay?  
40:19 A. Yes.  
40:20 Q. Why did Fannie Mae buy private  
40:21 label securities backed by subprime and Alt-A  
40:22 loans?  
40:23 A. For two reasons. First, and I  
40:24 think primarily, because those securities  
40:25 contributed positively to the company's  
  
41:2 housing goals, which I understand it was  
41:3 required to meet as a matter of law.  
41:4 And secondly, from time to  
41:5 time, because we believed at the time given  
41:6 the degree of credit enhancement in the  
41:7 securities, that they would provide a  
41:8 reasonable return to invested capital for the  
41:9 company's shareholders.